The Economist

Iraq's successful election
PAGE 43
The state of the union
PAGE 25
George Bush and Natan Sharansky
LEXINGTON, PAGE 32
Science, politics and climate change
PAGE 63

FEBRUARY 5TH–11TH 2005 www.economist.com

Love is in the air

The return of corporate mergers

US$4.95 • C$6.95

The Economist

FEBRUARY 5TH–11TH 2005 www.economist.com

A royal coup in Nepal
PAGE 25

Aid after the tsunami
PAGE 28

Corporate mergers are back
PAGES 10, 53 AND 60–62

Science, politics and climate change
PAGE 69

Heading back

But Thaksin's Thailand is a flawed model

The Economist

Iraq's successful election
PAGE 51

Blairites on a roll
BAGEHOT, PAGE 34

Corporate mergers are back
PAGES 10, 61 AND 67-69

Science, politics and climate change
PAGE 77

FEBRUARY 5TH-11TH 2005 www.economist.com

Taking Britain's liberties

£3.00 0.6
9 770013 061143

ONLINE FEATURES
Cities Guide Go
Country Briefings Go
Audio interviews Go
Classifieds Go

Full contents
Enlarge current cover
Past issues/regional covers

GLOBAL AGENDA
POLITICS THIS WEEK
BUSINESS THIS WEEK
OPINION
Leaders
Letters
WORLD
United States
The Americas
Asia
Middle East & Africa
Europe
Britain
Country Briefings
Cities Guide
SURVEYS
BUSINESS
Management Reading
Business Education
Executive Dialogue
FINANCE & ECONOMICS
Economics Focus
Economics A-Z
SCIENCE & TECHNOLOGY
Technology Quarterly
PEOPLE
Obituary
BOOKS & ARTS
Catch if you can
Style Guide
MARKETS & DATA
Weekly Indicators
Currencies
Big Mac Index
DIVERSIONS
RESEARCH TOOLS
CLASSIFIEDS
DELIVERY OPTIONS
E-mail Newsletters
Mobile Edition
RSS Feeds
The Economist Group
Economist Intelligence Unit
Economist Conferences
The World In
Intelligent Life
CFO
Roll Call
European Voice
Economist Diaries and Business Gifts

Advertisement

Print Edition February 5th 2005

Love is in the air
But will the latest flowering of corporate romance have a happy ending? ... More on this week's lead article

Previous print editions

Jan 29th 2005
Jan 22nd 2005
Jan 15th 2005
Jan 8th 2005
Jan 1st 2005

More print editions and covers »

Subscribe

Subscribe to the print edition
Or buy a Web subscription for full access online
RSS feeds
Receive this page by RSS feed

The world this week

Politics this week
Business this week

Leaders

Company mergers
Love is in the air

Anti-social behaviour in Britain
Taking liberties

Thailand
Heading back

China's exchange rate
Cock-a-doodle-doo

America in the Middle East
Night turns into day?

Sudan
Justice in Darfur

Letters

On corporate social responsibility, tort reform, Iraq's election, emerging-market debt

Special Report

Thailand's election
Thaksin's way

United States

State of the union
The revolution, phase two

The AARP
Still the biggest bruiser?

Paedophilia cases
Claims, counter-claims

Great American sports
You're chicken

Journalists, politicians and ethics
Fourth estate or fifth column?

Transport policy
The Windy City winds down

Lexington
The odd couple

The Americas

Mining in Peru
Halting the rush against gold

The World Social Forum
Utopia, meet reality

Brazil's central bank
Risks, new and old

Political succession in Jamaica
Moving on

Asia

Nepal
Feudal follies

China
The burial of Comrade Ziyang

China and Taiwan
A lunar thaw

Business

Corporate mergers
The fall of a corporate queen

Indian business
A splitting headache

European business subsidies
Neelie ventures forth

Europe's defence industry
The China syndrome

Fear of China
I spy spies

Retailing
Changing shopkeepers

Face value
Lord of the rings

Special Report

Consumer goods
The rise of the superbrands

Finance & Economics

The world economy
Still gushing forth

The G7 finance ministers' meeting
Africa expects

Citigroup and MetLife
Out of life

Marsh & McLennan
Settled, at a price

Municipal bonds
Let there be light

Reforming India's equity market
Loosening up

Plastic money
A durable idea

Economics focus
The economics of sharing

Science & Technology

Climate change and politics
Hotting up

Land-use change
Animal, farm

Neuroscience
Quieting the brain, opening the mind

Computer circuits
Barred and latched

The Richard Casement internship

Books & Arts

Slavery
Cruellest trade

The bicycle
Cranium cracker

Expressionist art

Japan
Metimorphosis

Australia
Guantánamo comes to Sydney

After the tsunami
The rebuilding starts

Middle East & Africa

Iraq's elections
Can the voters build on success?

Iraq's Kurds
They're on a roll, for now

Iraq's south
Worrying trends

The Arab neighbours
The fear of contagion

Land rights in Israel
Keeping control of Jerusalem

South Africa
Counting the cost of denial

Mozambique
The rights to prosper

Europe

German politics
The come-back chancellor

Denmark
Full Fogh forward

Europe's Roma
Poor and unloved

France and America
In search of repairs

Turkey's opposition
Time for a change

Charlemagne
Europe's dash for growth

Britain

Anti-social behaviour
Enemies of the state?

Naughty children
Not just William

Company taxation
Sparks fly

Animal-rights extremists
Flat-earth fighters

Private education
Breaking in

Wind farms
Breezy

Welfare reform
Off the sick

Public services
Never mind costs, feel the quality

Bagehot
Blairism triumphs, Gordon waits

Articles flagged with this icon are printed only in the British edition of *The Economist*

A fine line

Ian McEwan
The thinker

Richard Mabey
Healing force

Amazon worldwide bestsellers
The big book index

Obituary

Obituary
Miriam Rothschild

Economic and Financial Indicators

Overview

Output, demand and jobs

Prices and wages

Australia

Money and interest rates

The Economist commodity price index

Stockmarkets

Trade, exchange rates and budgets

Household debt

Emerging-Market Indicators

Overview

Emerging-market investment

Economy

Financial markets

Advertisement

Classifieds

Jobs
, P4 OSCE Secretariat Vacancy Number: VNSECP00127 Vacancy Notice Issue: 9 January 200....

Business / Consumer
A Leading Indian Recruitment and HR Consulting Firm is Looking for Partn....

Tenders
Business Opportunity - WSI Internet Start Your Own Business! Profit....

Jobs
LEADER OF COUNTRY STRATEGY PROGRAM In Nigeria (Ref # 05-156) IFPRI is an....

Business / Consumer
FOR SALE Specialist security fencing contracto....

Tenders
GLOBAL INVITATION FOR EXPRESSION ....

Sponsors' feature

document created by *NiflHeiM*

Politics this week

Feb 3rd 2005
From The Economist print edition

Iraq's elections

Getty Images

Elections in **Iraq** went better than many expected, with perhaps 60% of eligible Iraqis turning out, according to unofficial reports. Large majorities voted in Kurdish and Shia Arab areas, maybe a quarter of eligible voters in Sunni Arab ones. An Islamist-inclined, Shia-led list was expected to get the most votes, with a Kurdish alliance dominating in Kurdish areas. More than 265,000 expatriate Iraqis in 14 countries, including Iran, also cast ballots.

All the same, the 260 **insurgent attacks** recorded in Iraq on polling day were the largest number since the Americans invaded nearly two years ago: at least 44 people were killed, including insurgents and ten British servicemen who died when a C-130 transport plane crashed. Two insurgent groups claimed separately to have shot it down.

See article

Israeli and Palestinian leaders said they would meet for a **summit** next week in Egypt, holding out the promise of a formal ceasefire.

The report of a UN commission on the western Sudanese province of **Darfur**, where some 70,000 villagers have been killed by government-sponsored militias, found no clear evidence of genocide but said that “no less serious and heinous” crimes had been perpetrated.

See article

As *The Economist* went to press, an independent inquiry under Paul Volcker was poised to report on the UN's **oil-for-food** scandal. It was expected to accuse Benon Sevan, director of the Iraq programme, of a serious conflict of interest, and to criticise the UN's auditing procedures. The inquiry will look at the role of Kofi Annan, the secretary-general, in a later report.

Zimbabwe's government said a general election would be held on March 31st. A group of 20 South African trade union leaders, allied to South Africa's ruling African National Congress, arrived in Harare, Zimbabwe's capital, hoping to check if conditions existed for a fair poll. They were promptly deported.

Prayers and reassurance

The long-ailing **Pope John Paul II** was rushed to hospital after suffering breathing difficulties. The Vatican later said that the 84-year-old pontiff's condition had stabilised.

German unemployment went above 5m in January, its highest level since the 1930s—although the figures are not seasonally adjusted, and were also boosted by the impact of the Hartz labour-market reforms in January.

See article

Spain's parliament rejected a proposal by **the Basques** to stage a referendum on their right to form a free state. The Basque premier said that he would hold the referendum, which has been approved by the Basque regional parliament, anyway. He also brought forward Basque elections to April 17th.

The **Irish Republican Army** delivered a blow to the Northern Ireland peace process by withdrawing an offer to decommission arms. The British government recently blamed the IRA for the province's biggest ever bank robbery.

The European Commission warned **Croatia** that it would not recommend the start of EU membership talks, scheduled in March, unless the Croatians handed over an indicted general to the war-crimes tribunal in The Hague.

Slovenia became the third European Union member to ratify the draft **EU constitution**, after Lithuania and Hungary. At least nine members plan to hold referendums on the constitution, starting with Spain on February 20th.

Georgia's prime minister, Zurab Zhvania, was found dead in an apartment in Tbilisi, apparently poisoned by a leak from a gas heater.

Talking the talk

George Bush delivered his annual **state-of-the-union** address to Congress. His main themes were the continuing push for democracy in the Middle East and reform of Social Security at home.

See article

A federal judge ruled that tribunals set up to review the status of prisoners at **Guantánamo Bay** are unconstitutional and unfair. This week's ruling contrasts with another decision, made by a judge in the same court last month, which said the detainees have no rights under the American constitution. The issue is expected to go to appeal.

Sam Bodman was confirmed by the Senate as **energy** secretary. Mr Bodman has to push the administration's stalled energy bill through Congress and will rejoin the battle to open an Alaskan wildlife refuge to oil production.

Jury selection began in the so-called “trial of the century”. **Michael Jackson**, a pop-star phenomenon, is accused of molesting children at his ranch; he says he is innocent.

Return to form

In **Colombia**, 23 troops were killed in two attacks by FARC guerrillas in as many days in the country's south-west. It was the worst setback for the armed forces since Álvaro Uribe became Colombia's president in 2002.

Venezuela's leftist president, Hugo Chávez, said he was looking to sell eight oil refineries in the United States owned by PDVSA, the state oil firm, as part of a policy to redirect Venezuela's oil sales away from the American market. PDVSA later said it had not yet decided.

The European Union's foreign ministers approved a plan to restore normal diplomatic relations with **Cuba's** communist government. This ended a “cocktail party war” that began in 2003 when Cuba jailed 75 domestic opponents and embassies infuriated Fidel Castro by inviting dissidents to receptions.

Monarchical ruling

Reuters

Nepal's monarch, King Gyanendra, staged a coup by dismissing the government and declaring a state of emergency. He then installed a new cabinet under his personal direction. He claimed the previous government had failed to deal with Nepal's many problems, most notably the country's Maoist insurgency.

See article

Zhao Ziyang, the former general secretary of **China's** Communist Party, purged for his sympathies with the Tiananmen students, was buried in Beijing. The ceremony was neither a private affair nor a state one, but reflected an uneasy compromise.

See article

Tests were said to have shown strong signs that uranium hexafluoride surrendered to international inspectors by Libya last year came from **North Korea**.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Business this week

Feb 3rd 2005
From The Economist print edition

Proctor & Gamble gets bigger

America's largest producer of household goods, **Procter & Gamble**, agreed to buy **Gillette**, a maker of razors and batteries, for $57 billion. The merger, one of the largest ever, will create the world's biggest consumer-goods business, and should provide more clout for the supplier in price negotiations with mega-retailers such as Wal-Mart.

See article

SBC Communications announced a merger with **AT&T** for around $16 billion. The deal needs to be approved by almost 30 state regulators, and is not expected to be completed until 2006. Speculation mounted that America's largest telecoms company, Verizon, would try to shore up its position by acquiring MCI or Sprint.

See article

Citigroup said it was selling its **Travelers** life-insurance business to MetLife in a deal worth $11.5 billion. The deal completes the reversal of a grand banking-and-insurance merger in 1998.

See article

Shareholders at **Adolph Coors**, a Colorado-based brewing company, approved a $3.4 billion merger with **Molson**, a Canadian brewing company. Molson Coors will become the world's fifth-largest brewer.

The growth engine

Surpassing all forecasts, **Google's** profit surged to $204m in the three months ended December 31st (compared with $27m for the same period in the previous year), helped by an increase in traffic and advertising revenues from its internet search engine over the Christmas season.

The world's largest private-sector oil company, **Exxon Mobil**, posted a fourth-quarter profit of $8.4 billion, a year-on-year rise of 27%. Full-year profit for 2004 was $25.3 billion. The Texas giant is yet another oil firm to reap a windfall from last year's surge in oil prices: Royal Dutch/Shell, ChevronTexaco and ConocoPhillips have all reported that their fourth-quarter profits roughly doubled.

Bolstered by strong DVD sales and advertising on its cable channels, **News Corp** said revenue had increased by 18% year-on-year in the quarter ending December. Net income rose to $386m, from $215m.

Walt Disney announced a 5% increase in net income for the last three months of 2004 compared with the same period in 2003. The conglomerate's profits were augmented by an 11% rise in revenue from its media networks and a 30% rise in revenue from theme parks and resorts.

Italian take-away

Sikorsky lost a hotly contested contract to build America's "Marine One" presidential helicopters. The new helicopters will be built by an international team led by Lockheed Martin based on a design by AgustaWestland, an arm of the Italian defence firm Finmeccanica. The $6 billion contract has been decried by some congressmen as "outsourcing".

Boeing's fourth-quarter profits nosedived to $186m from $1.1 billion a year earlier. However, indications of brighter skies ahead came with news that six Chinese airlines had agreed to purchase 60 of Boeing's new aircraft, the 787.

An unusual agreement by ten **WorldCom** directors to pay $18m of their own money in settlement of a class-action lawsuit by shareholders of the once-bankrupt telecoms giant collapsed after the judge rejected a provision in the deal.

The world's largest insurance broker, **Marsh & McLennan**, agreed to pay $850m (in instalments) to settle civil charges that it rigged bids and acted against its clients' interests. The firm, investigated by Eliot Spitzer, New York's attorney-general, agreed to apologise to clients for "shameful" acts, but did not admit (or deny) any wrongdoing.

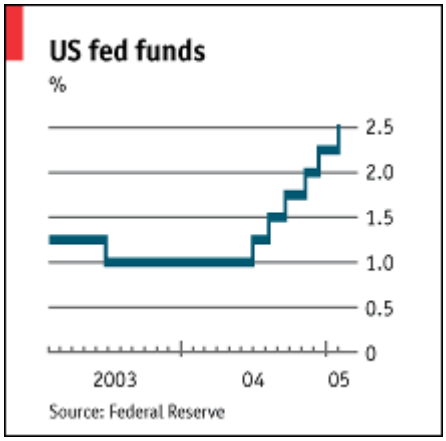
See article

The **New York Stock Exchange** released a report criticising the methods by which Richard Grasso, its former chairman and chief executive, was able to set his controversial $187.5m compensation package. Mr Grasso is being sued (by the ubiquitous Mr Spitzer) for the return of some of the money.

Russia's economy received a fillip as Standard & Poor's raised the country's long-term foreign-currency sovereign credit-rating from "junk" to investment grade. Russia became a net creditor at the end of 2004 (helped in part by high oil prices). S&P'S decision follows on the heels of similar upgrades by both Fitch and Moody's.

Managed expectations

In a widely expected move, America's Federal Reserve put up its key **interest rate** by one-quarter of a percentage point to 2.5%, the sixth rise since last summer. A weak dollar and surging oil prices underpinned concerns that inflation might continue on its upward path. The Fed made the now familiar statement that its response was "measured".



Company mergers

Love is in the air

Feb 3rd 2005
From The Economist print edition

But will the latest flowering of corporate romance have a happy ending?

AFTER a miserable few years in the executive suite, with only the ugly sisters of cost control and corporate governance for company, many a boss's thoughts have lately turned to love. A recent spate of headline-grabbing mergers seems to herald another wave of corporate marriages. The mood had already begun to sweeten last year, the most active for mergers and acquisitions (M&A) worldwide by value since the last wave broke in 2000. But the recently announced nuptials of some of the world's most celebrated firms—Procter & Gamble (P&G) tying the knot with Gillette, “Ma Bell” (AT&T) being swept (a tad Oedipally) off her feet by one of her own “Baby Bells”, SBC—have once again given the urge to merge the aura of respectability in the corporate world, a respectability lost when so many of the previous wave of beautiful marriages (remember AOL-Time Warner?) crashed so soon and so spectacularly on to the rocks.

Falling in love is often a triumph of hope over experience—and the history of mergers contains enough tragedy to terrify the most resilient romantic. The diversification wave on both sides of the Atlantic in the 1960s and 1970s famously ended in tears and break-ups. Yet despite claims that lessons had been learnt, the 1990s merger wave was as damaging as any before it. Shareholders in acquiring firms typically gain less from mergers than shareholders in acquired firms. But in 1991-2001, according to a study by René Stulz of Ohio State University and two fellow economists, in the three days following American merger announcements, acquiring shareholders lost $216 billion—over 50 times what they lost in real terms in the 1980s, though they spent only six times as much. (The results are no better over longer time periods.) Strikingly, these losses were concentrated in just 87 big deals in 1998-2001. In total, mergers during that period actually destroyed some $134 billion of shareholder wealth.

In the mood

Will the current wave of mergers produce a happier ending than its predecessors? Many of the most disastrous mergers have been the result of a chief executive's excessive ambition (for instance, ill-fated empire-building such as Daimler boss Jürgen Schrempp's purchase of Chrysler) or of his desperation (intense pressure on Time Warner's Gerry Levin to embrace the internet led to the merger with AOL). In the past few years there has been so much hostility to M&A from investors and outside directors that the typical boss would sooner have proposed giving up his corporate jet than doing a merger. Now, with profits booming, balance sheets (mostly)

strengthened and corporate-governance reforms implemented, investors and outside directors are increasingly asking the boss not what he is doing to get the firm back on track but how he plans to expand it. In this environment, a merger proposal may, once again, be enthusiastically received.

Much will depend, then, on whether bosses have curbed their imperial ambitions enough to propose only deals that truly make business sense—and on whether boards and investors have mustered the courage to question a boss's merger plans thoroughly or, equally, not to put him under such pressure that he proposes a merger out of desperation. And even if the balance of power is healthier than in the past, it remains to be seen whether shareholders or chief executives, acting together, are any better able than their predecessors to spot the difference between a faddish merger and a useful one.

One hope that they might be more skilful lies in changes to executive compensation. Linking a boss's reward to his firm's share price was supposed to deter him from mergers that destroyed shareholder value. Alas, during the 1990s, the link was often to short-term changes in share prices; when M&A was briefly fashionable, this rewarded acquisitive bosses handsomely but prematurely. If it is true, as is widely claimed, that executive remuneration is now more closely linked to the creation of long-term shareholder value—the formulas are often so complex that this is difficult to determine—then bosses may indeed become more selective in the mergers they propose.

Questions of focus

So far, the recent merger activity has mostly been characterised by the sort of focused deals that experience suggests are likeliest to create shareholder value. (However, on past experience at least, the growing use of shares, rather than cash, as payment is a bad sign.) P&G's acquisition of Gillette (see article) and SBC's purchase of AT&T (see article) were driven by cost-saving rationalisation within an industry. Another deal this week, the sale of Citigroup's Travelers Insurance arm to MetLife (see article), another insurer, is at once both a focused, rationalising deal for MetLife and evidence that Citi is abandoning some of the grander ambitions of Sandy Weill, the erstwhile corporate empire-builder responsible for the merger of Travelers and Citibank in 1998.

Arguably, opportunities now abound for focused mergers, above all in globalising industries with excess capacity such as consumer goods, telecoms and banking. European firms, in particular, are far more diverse than their American counterparts, and face pressure from shareholders to become focused, not least by selling non-core businesses. The degree of conglomeration in Europe today is similar to that in America in the 1980s before a wave of rationalising mergers which produced both better-managed firms and real economic gains.

The emergence of big private equity firms—which now account for a growing slice of M&A activity—is making it much easier for firms to sell their non-core businesses, and for corporate buyers such as P&G to offload quickly unwanted parts of an acquisition (Gillette's Duracell battery business perhaps). Increasingly, bidders work with private-equity firms to carve up a target before a deal is done, which increases the likelihood of success.

Yet merger waves usually begin for the right reasons, only for bidders to be caught up in the thrill of the chase—waking up to a nasty shock the morning after. Sooner or later, alas, the same is likely to be true of the current wave of mergers, too.

Anti-social behaviour in Britain

Taking liberties

Feb 3rd 2005
From The Economist print edition

What the war on terror and the war on anti-social behaviour have in common

Get article background

WHAT'S a government to do when faced with a bunch of undesirables whose guilt is difficult to prove in a court of justice? Lock them up without a proper trial, of course.

That's how the British government is dealing with people it suspects of terrorism. Its actions, including its shocking announcement last week of a new power of house arrest, have rightly been condemned as an attack on civil liberties. But cases of suspected terrorism are not the only ones in which the principles of the criminal justice system have been abandoned. The state has given itself new powers to deal with minor offences and other crimes which are scarcely less draconian than those to deal with suspected terrorism.

Over the past decade, anti-social behaviour—hellish neighbours, beggars, teenage gangs—has become a big worry in Britain (see article). Rightly or wrongly, people think that drunkards and beggars are more aggressive these days, that teenagers are more threatening and that bad children have got worse. Explanations vary, with some blaming 1960s liberalism and others 1980s individualism. But all agree that the normal remedies for dealing with neighbourhood tyrants are not up to the task. The police lack the time to collect evidence; witnesses are too scared to testify; wrongdoing is difficult to prove; and sentences are too mild.

In response to such difficulties, the government has created a new set of legal tools. Chief among them is the anti-social behaviour order, or ASBO. This is a list of restrictions tailored to an individual offender that can now be obtained either in a civil hearing or following a criminal conviction.

Troublemakers as young as ten years old can be barred from entering neighbourhoods, ringing doorbells, using public transport and mobile phones or even uttering certain words for a minimum of two years. Securing an ASBO is easy. Hearsay evidence, for instance, is admissible in court. The consequences of stepping out of line are weighty: a maximum of five years in prison for doing something that is not necessarily an offence in law. Not surprisingly, such a powerful weapon is popular: more than a thousand ASBOs were handed out in the first half of 2004.

That delights MPs, who were sick of hearing stories from their constituents about local teenagers who have terrorised the neighbourhood by blasting music, breaking windows and spitting at passers-by. Prosecutors and the police are also pleased. Their powers to deal with low-level offences used to be weak. Now they are so draconian that they undermine the principles on which the criminal justice system is built.

Trust us

The power to obtain anti-social behaviour orders was granted to the police and local authorities on the assumption that they were to be used with restraint. Just as the government promises to subject only genuinely scary terrorists to house arrest, so the forces of law and order are supposed to aim their most potent weapon only at the most dedicated and egregious troublemakers. Don't worry, goes the typically British assurance: our powers may be draconian, but decency and common sense will ensure we don't overuse them.

That's not what has happened. Obtaining an ASBO is so easy (fewer than one in 70 applications are turned down) that they have been used to tackle a wide range of undesirable behaviour. ASBOs allow the police to nail people for offences too minor to be criminal. Orders have been secured against crotchety old neighbours, prostitutes, beggars and mothers who argue with their children. Some of these people have subsequently been jailed for breaching their ASBOs: most absurdly, one man was sentenced to four months in prison for howling like a werewolf.

More worryingly, ASBOs allow the police to bypass the normal procedures of criminal justice when they suspect somebody of serious criminal activity but can't prove it. A suspected drug dealer, for instance, can be banned from using a mobile phone—a crucial tool, in his supposed profession. When he is caught doing so, he can be jailed.

If it's broke, fix it

It is not surprising that ASBOs are being used so frequently and so unwisely. After all, the English legal system is founded not on the assumption that everybody will behave with decency and restraint but on the rather more reliable conviction that most people, including the police, are capable of lying and may do so if it is to their advantage. Faced with two competing accounts of what one person has done to another, the courts normally give both of them a hard time. Accusations are minutely examined; witnesses are accused of fabricating their stories. Fail to make your case and you lose.

As the police point out in defence of their enthusiasm for ASBOs, the criminal justice system does not always work well. If the police catch villains, prosecutors sometimes don't charge them; if they charge them, witnesses don't turn up to give evidence; if witnesses do turn up, the case is all too often adjourned because the courts' administration is chaotic. These are, indeed, serious problems; but the government needs to deal with them, not create new, lazy ways around them. The safeguards built into the criminal justice system are there for a good reason. If the police think a man is a drug dealer but can't prove it, he shouldn't go to jail, however often he uses his

mobile phone.

The defence of civil liberties is rarely a vote-winner. People are, understandably, moved more easily by violence against people than by attacks on systems. Politicians are keener to be seen to be protecting victims than defending the rights of suspects. In a country without a written constitution, the rules that underlie a properly-run society are particularly vulnerable to the whims of populist politicians, and vigilance is therefore especially important.

Britons are lucky people, and complacent ones. The liberties they take for granted have evolved over a thousand years or so. The idea that any one government should seriously undermine them seems implausible. It isn't.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Thailand

Heading back

Feb 3rd 2005
From The Economist print edition

He's cruising to re-election, but Thaksin's Thailand is a flawed model for South-East Asia

Get article background

WE OWE Thaksin Shinawatra, Thailand's prime minister, an apology. Four years ago, when he won his first election, *The Economist* was sceptical (see article). We said his position as Thailand's richest man exposed him to insuperable conflicts of interest, that his instincts were alarmingly undemocratic and that his populist election promises were unrealistic and bound to produce either disappointment or real economic damage. As Thailand votes again, on February 6th—with Mr Thaksin reckoned to be sure of increasing his mandate—we are happy to revise this assessment.

Against our expectations, Mr Thaksin has managed broadly to keep his election promises, which centred on three give-aways (cheap health care, debt forgiveness for farmers and micro-credit for villages), while not in the process inflating Thailand's borrowing to dangerous levels. A booming economy, for which Mr Thaksin deserves at least some of the credit, has made this possible. Though more debt than is admitted to may have been squirrelled away off the national balance sheet, our fears on the economy have proved exaggerated. On other fronts, however, Mr Thaksin continues to look as guilty as charged (see article).

Take conflicts of interest first. Mr Thaksin complied with the law by divesting himself of all his holdings—but only by transferring them to other family members. They still hold big stakes in Shin Corporation, the holding company he set up. This gives the family stakes in Thailand's biggest mobile-phone company and its only commercial satellite operator (Mr Thaksin made the fortune that allowed him to enter politics in telecoms), not to mention a television channel, an internet service provider, an advertising firm, an airline and a property developer, as well as similar investments in neighbouring countries. The prime minister denies abusing his position to benefit

these companies in any way. But several questionable cases have raised eyebrows, and Thailand lacks the formal oversight or control mechanisms that are needed to ensure that favouritism cannot occur.

However, the more telling charge to be laid against Mr Thaksin is not so much what he has done as what he has not done. A great deal of Thai commerce remains a cosy oligopoly run by a handful of huge family-owned businesses, of which Shin Corp is one. Mr Thaksin has not initiated nearly enough of the deregulation, privatisation or opening to foreign competition that Thailand needs to assure its longer-term future. True, the record in most of the rest of South-East Asia is no better. But the whole point of putting a businessman in charge of the economy ought to have been to make Thailand's economy more competitive.

Nor should anyone be happier than we were four years ago about Mr Thaksin's respect for democracy. In office, he has behaved more like an unelected strongman than a parliamentarian. His hatred of criticism is legendary. He and his associates are accused of using their power and money to discourage dissent. Shin Corp, for example, bought control of Thailand's only independent television station before the 2001 election. Since then, relatives of the secretary-general of Mr Thaksin's party have bought a big stake in the country's most outspoken newspaper, the *Nation*. In the past four years, the safeguards built into Thailand's 1997 constitution, especially the constitutional court and the counter-corruption commission, have been weakened. Mr Thaksin has appointed his cousin to head the armed forces. Unconstrained by the niceties that would obtain in a country protected by a vigorous rule of law, his government has got away with some extremely unpleasant actions. Around 2,000 supposed dealers were killed during Mr Thaksin's (literal) war on drugs. The government says they were killed by their own to avoid confession, but many human-rights groups say they were killed by the police. In the south, the security forces have dealt brutally and incompetently with Muslim separatists, and a full-blown insurrection looms. Yet Mr Thaksin airily brushes such matters aside.

The prime minister's supporters do not seem to care. Has not their man delivered firm government in place of the weak and shifting coalitions of the past—governments whose incompetence opened the way to bouts of military rule and helped to produce Asia's economic crisis of the 1990s? The memory of the chaos that preceded him, plus the favours he has doled out to Thailand's farmers, will doubtless ensure his re-election with a handsome majority.

The perils of stability

It is true that Mr Thaksin has brought stability. His is the first democratic government to last a full term in Thailand. Compare the country with some of its neighbours, such as the Philippines and particularly Indonesia—now on its fifth president in six years—and continuity might seem no bad thing.

But stability is not everything. Thailand's closest neighbours are Malaysia, Laos, Myanmar and Cambodia, all of which demonstrate that continuity of government has drawbacks as well as strengths. Stable government can bring stultification, and the cementing into place of powerful forces whose interests are best served by allowing change to occur slowly, if at all. The shame of South-East Asia is that no country has yet achieved a truly competitive multi-party system, where voters are offered clear alternatives. In places where elections take place, virtual one-party states, such as in Singapore, or weak coalitions seem to represent the only alternatives. Thailand has come closest to offering a clear choice, pitting Mr Thaksin's well-defined nationalist and populist party against the technocratic and progressive Democrats. But the success of the fabulously rich Mr Thaksin threatens to drive Thailand back towards the single-party model.

Successful democracies require checks and balances, and the biggest worries about Mr Thaksin all

relate to the absence of them. Ideally, the opposition would fill the gap. But the Democrats are unlikely to be in a position to do so after Saturday's election. A weakness for strong men does Thailand few favours. Its democracy will not be mature until it embraces the orderly rotation of coherent governments.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

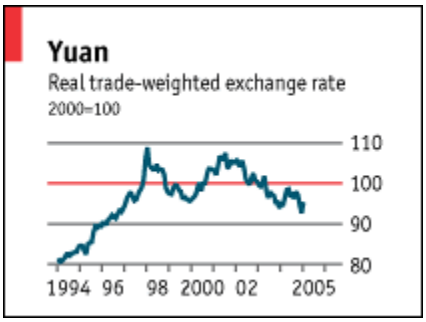
China's exchange rate

Cock-a-doodle-doo

Feb 3rd 2005
From The Economist print edition

The cure for America's trade deficit lies with its economic policy, not China's exchange rate

Get article background



ON FEBRUARY 9th the Chinese new year begins: the year of the rooster. Many western policy makers and businessmen hope that a new year will encourage new thinking in Beijing to revalue the Chinese yuan, which is pegged to the falling dollar. The yuan, it is widely argued, is grossly undervalued and represents the biggest obstacle to a reduction in America's huge current-account deficit. China has been invited to the G7 meeting of finance ministers and central bankers in London this weekend, where it is likely to come under pressure to adjust its exchange rate. But the G7 members should save their breath: not only would a revaluation of the yuan have little impact on America's deficit, but the more that foreigners pressure China to act, the harder it is for China do so.

To begin with, it is not obvious that the yuan is undervalued. The surge in China's foreign-exchange reserves suggests that the yuan is being held down, but this largely reflects short-term capital inflows from investors speculating on a revaluation; these flows could go into reverse. Moreover, if the yuan were set free and capital controls scrapped, the currency might fall as Chinese households and firms diversified into foreign assets. And while it is true that the yuan's trade-weighted value has recently fallen along with the dollar, this follows a period when the yuan was dragged up by a rising dollar: from 1994 to 2001 its real trade-weighted exchange rate gained 30%. Given the uncertainty about the yuan's correct level, it makes more sense to focus on how China can move to a flexible exchange-rate regime—to which its government is committed—than to insist on a specific yuan revaluation.

In any case, a revaluation is not, as commonly claimed, the vital element needed to shrink America's trade deficit. China accounts for only 10% of America's total trade, so a 10% revaluation would reduce the dollar's trade-weighted value by a mere 1%. More generally, although a fall in the dollar is necessary to reduce America's deficit, it is not sufficient. The real solution lies at home: the American government needs to borrow less and households must save more and spend less.

On the other hand, it is in China's own long-term interest to move to a more flexible exchange rate. This would give it more control over monetary policy. By fixing its currency to the dollar it is, in effect, being forced to adopt America's overly lax policy. Inflation is not currently a problem (it has fallen from 5% to 2.4% over the past six months), but ridiculously low real interest rates in a fast-growing economy are likely to cause a misallocation of credit and to fuel investment and property bubbles. A more flexible exchange rate would also help to buffer the economy against shocks. But the timing of any change is tricky. A modest currency adjustment at a time of strong

speculation could attract yet bigger inflows of hot money, as investors bet on further appreciation. Last week, Li Ruogu, the deputy governor of the central bank, made clear that China would adopt a more flexible exchange rate, but in its own time, not under pressure.

A first step towards flexibility might be for China to peg the yuan to a basket of currencies rather than to the dollar. One result would be China reducing future purchases of American government bonds. Yields on these would rise. This would, indeed, help to reduce America's trade deficit, but in a much more painful way than those who call for a yuan revaluation have in mind. The year of the rooster may yet deliver a wake-up call, but to America rather than to China.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

America in the Middle East

Night turns into day?

Feb 3rd 2005
From The Economist print edition

Not quite yet

AFP

POOR Condi. America's new secretary of state makes her first visit to the Middle East this week in what a cynic might consider the worst possible circumstances: a climate of sudden optimism. In Iraq last weekend millions of people defied the threats of the insurgents and trekked to the polling stations to take part in the first free vote of their lifetimes. At the same time, a new coalition government in Israel and a new Palestinian president are showering one another with praise and encouragement in place of the customary missiles and mortars. On both flanks of the region cliché-writers are hard at work turning corners and flinging open windows of opportunity. Is there (let's join the club) sudden light at the end of the tunnel?

Perhaps—but the tunnel is long. Condoleezza Rice has enough experience to know that sudden turns for the better are seldom the way of the Middle East. Her first job as secretary of state is therefore to adjust expectations without squashing hope. This is not because the success of Iraq's election or the new mood in Palestine are illusory. They are real enough, and present real opportunities. But if America is to exploit these opportunities it will need to apply imagination, staying-power and a precision of manoeuvre that was often absent during George Bush's first term. In Iraq and Palestine alike, the obstacles remain daunting.

Take Iraq first. In many ways, the election was a marvel. The fact that so many Shias and Kurds trooped to vote (see article) proves that most Iraqis endorse the American-led and UN-endorsed plan for their future and repudiate the “resistance” that had presumed to murder in their name. This should boost Ms Rice's ability to collect support for America's Iraq policy in Europe and in the wider Arab world. Inside Iraq itself, the visible success of the election should stiffen the spine and broaden the appeal of a fresh government armed with a precious new asset—a democratic

mandate.

All that is good. The less good countervailing fact is that the Americans still have an insurgency to defeat. And although the election has exposed the isolation of the mostly Sunni insurgents, it may in the short run have the effect of inspiring them to redouble their attacks on a new order in which they see power slipping away via the ballot box to the Shia majority. Until the United States finishes the job of training Iraq's new soldiers and policemen, the United States will therefore find itself in the awkward position of fighting in the service of an Iraqi government whose values and instincts may—nobody yet can tell—turn out to have rather more in common with those of Shia Iran than America's own.

Ms Rice will be flying into some dangerously elevated expectations in Palestine too. It is excellent that Mahmoud Abbas, Yasser Arafat's successor, is breaking out of the vicious circle of the *intifada*, talking the armed factions into ceasing fire and so setting the scene not only for a tentative, reciprocal ceasefire from Israel but also for a meeting next week with Israel's prime minister, Ariel Sharon. As so often in this conflict, Israelis and Palestinians are bending over backwards to show a newly engaged American administration that their side is sweetly reasonable. This is an opportunity Ms Rice should use to ease Israel's promised withdrawal from Gaza and make it clear that Mr Bush expects it eventually to withdraw from most if not all of the West Bank too. At the very least she needs to insist on both sides taking their first step along the so-called “road map” by stopping the killing and, in Israel's case, freezing settlement expansion in the West Bank.

As in Iraq, however, the underlying obstacles have changed less than the surface mood. Mr Abbas cannot immediately impose quiet in Palestine if the radicals of Hamas choose to oppose him. Iraq's government cannot suppress its insurgency unaided. The jobs of partitioning Palestine peacefully into two states and maintaining Iraq as one will be the work of years, not months. Above all else, Ms Rice should use her maiden voyage to persuade the doubters that America has the will and the patience to see both sides of the business through.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Sudan

Justice in Darfur

Feb 3rd 2005
From The Economist print edition

Why America should give a chance to the International Criminal Court

EPA

Get article background

"NEVER again", the world said after the Holocaust. "Never again", it repeated after Cambodia, Bosnia, Rwanda. Yet two years after the beginning of another potentially genocidal conflict in Sudan's western province of Darfur that has already claimed 70,000 lives and driven nearly 2m from their homes, the world is again standing idly by. Despite a UN Security Council resolution last July promising to do everything possible, little has been done: no military intervention bar a token force of 1,000-odd soldiers from the African Union, no UN sanctions, no punitive measures of any kind. Yet some 10,000 lives are still being lost every month as the bombing, slaughter and rape continue.

The publication this week of a long-awaited report from a UN commission on Darfur offers a new opportunity for action. Although it found no clear evidence of genocide, it says that "no less serious and heinous" crimes have been perpetrated. Laying the blame on all parties to the conflict, it "strongly recommends" that the Security Council refer the situation to the International Criminal Court (ICC) for possible prosecution of the guilty.

This would be a first for the world's first permanent war-crimes court. But it poses a dilemma for the United States. As the only country to have declared that the atrocities in Darfur amount to genocide, it has been in the forefront of those pressing for tougher action against Sudan and "accountability" for the perpetrators. But it strongly opposes what President George Bush has castigated as "a foreign court...where unaccountable judges [could] put our troops and officials at an unacceptable risk of politically-motivated prosecutions."

Protesting that the United States does not want to be “party to legitimising the ICC”, American officials propose setting up instead an ad hoc tribunal based in Tanzania under the auspices of the African Union to try those responsible. But this would waste time and money. The ICC, which is already up and running, was tailor-made to address cases such as this.

Since the United States withdrew its signature from the ICC in May 2002, it has waged a relentless campaign against the court, threatening to cut American aid to countries which have ratified its statutes unless they sign bilateral agreements pledging not to hand over American suspects to the court. It has also tried to press the Security Council into granting its citizens blanket immunity from the court, threatening to withdraw its support from UN peacekeeping missions unless it did so.

And yet America has little need to fear the court. Its statutes already contain ample safeguards to protect every country against frivolous prosecutions. Under the “principle of complementarity”, it may try someone only if their own country is genuinely unable or unwilling to do so. Only if the investigations are deemed bogus and designed solely to shield the suspect from criminal responsibility can the ICC intervene. Even then, a seven-judge pre-trial chamber must decide that there are “reasonable” grounds. All troops involved in UN peacekeeping missions are exempt from prosecution.

Of the 139 countries which have signed up to the ICC, 97 have so far become full “state parties” after ratifying its statutes. They include all 25 members of the European Union, all of America's NATO partners bar Turkey, and nine of the Security Council's 15 members. Mr Bush cannot easily do an about-turn on the ICC. But by abstaining on a resolution that referred Darfur to the court, he could still help the cause of justice.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Letters

Feb 3rd 2005
From Economist.com

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

The good company

SIR – Your survey of corporate social responsibility (January 22nd) argues that governments should be accountable only to their electorates and managers only to their shareholders. However, governments have become frequently accountable to certain parts of their electorates more than others. Consequently, a large and well-organised set of consumers does not see its priorities reflected in the policy actions of its governments. These global citizen-consumers have come to believe that they can exert influence over public policy more effectively through consumer activism. When large numbers of consumers come to believe this and act accordingly, managers practise "good management"– not "delusional CSR".

Raymond Levitt
Stanford, California

SIR – Your arid leader ("The good company", January 22nd) seeks to discredit CSR by creating a false antithesis. Most advocates of CSR accept, as I do, that unadorned capitalism can serve the public interest — and adorned capitalism, through companies with an appropriate and proportionate approach to CSR, can serve that interest even better. The impact on reputation, on recruitment and on potential investors is considerable. You are right to remind us that corporate giving is philanthropy at shareholders' expense and that concentration on shareholders' interests is the first responsibility of management. It is, however, wrong to suggest that the two are irreconcilable. I firmly believe that the best companies, in Adam Smith's terms, can also be "good" and that your pejorative use of that adjective is misguided.

Sir Christopher Bland
Chairman, BT Group
London

SIR – The idea that unregulated capitalism automatically generates social benefit is nonsense. Irresponsible companies cause damage by pursuing profit at the expense of everything else. Such companies do not simply ignore the social implications of their actions; they knowingly pursue strategies that will be harmful. However, not all NGOs are anti-capitalist. We simply demand that businesses ensure their operations do no harm to vulnerable people or environments and operate to high standards wherever they work, whether in pharmaceuticals, mining, sweatshops or commodity supply chains.

Jeremy Hobbs
Oxfam International
Oxford, Oxfordshire

SIR – The very first food aid to arrive in tsunami-stricken Banda Aceh from the World Food Programme was trucked in by a corporate donor. TNT provided aircraft, delivery vans and drivers. Unilever lent its vast distribution network to get food to survivors. Danone manufactured and donated high-energy biscuits. Citigroup immediately offered office space, desks and phones for the team of WFP logisticians. And Boston Consulting Group employees lent their expertise. In the immediate aftermath of a disaster, this kind of help is better than any money can buy.

James Morris
UN World Food Programme
Rome

SIR – A well-run company engaging in the selfish pursuit of profit would lobby for subsidies and tariffs to reduce costs and increase revenue, heedless of the market distortions they may cause. How do you square this with your usual argument that free trade is necessary to lift developing countries out of poverty?

Jean-Philippe Marcotte
San Francisco

SIR – Like the academics and consultants that have mushroomed under CSR, you concentrate on a woolly debate and wholly ignore the challenge that capitalism faces today. There is a prevailing public distrust of companies arising from the perception that profit precedes principle, rather than being based upon it. Nothing could better illustrate the validity of this perception than the recent 20th anniversary of the Bhopal disaster — one of the worst examples of compromised safety and adequate compensation being denied in the interest of corporate profit. Capitalism, the most effective mechanism the world has so far known for providing goods and services and creating wealth, is under threat not from without, but from itself and from its lack of underlying principles. It is a threat probably increased by the confusion of thought fostered by the proponents of CSR and the tunnel vision of its opponents, whose views dominated your survey.

Sir Geoffrey Chandler
Former Director,
Shell International
Dorking, Surrey

SIR – Governments fail to pass adequate laws to protect the environment, contribute miserly sums to relieve tragedies and tolerate or exacerbate the existence of extreme poverty. The fact that some corporations have chosen to devote assets to their social responsibilities is far less troubling than the fact that some governments have not.

Pat Meier
Blanchardville, Wisconsin

SIR – As companies have gone global, issues once considered “soft” by the private sector now pose “hard” business dilemmas and are becoming part and parcel of corporate risk analysis. So long as governments fail to do their part and so long as business goes global, CSR helps fill an important void.

Georg Kell
UN Global Compact
New York

SIR – There you go, comparing Adam Smith's butcher, brewer and baker with multinational conglomerates. This is ridiculous. Then as now, neighbourhood butchers do not command multi-

million dollar advertising campaigns, experts to move pre-tax profits to no-tax havens, and the clout to lobby politicians on national, or even local, issues. Neither Smith's, nor today's, butcher can get huge tax breaks and heavy subsidies on top. Nor do they command annual budgets that exceed the GDP of small countries.

Martina Hütter
Hamburg, Germany

SIR – At the heart of the issue lies pressure from those NGOs to whom modern capitalism and profitmaking are anathema. They have been remarkably successful at gaining the moral high ground (they are even dubbed a "civil society") and in nurturing a distrust of business. This in turn has led business to distrust itself, producing a climate in which companies rush to embrace all aspects of the CSR agenda. The challenge now is to generate a new climate where business considers what the right elements to pursue under the heading of "good management" are. If that cannot be achieved, more regulation will inevitably move the equation inexorably from good management, within the control of business, to pernicious and delusional CSR.

Patricia Peter
Institute of Directors
London

SIR – As a consumer and a citizen I must say that neither hamburger chains sponsoring youth football teams nor the occasional recycled envelope impresses me much. Companies should drop this fashionable farce. Or at least call CSR by its true name: marketing.

Ingvild Paulsen
Glasgow

SIR – It seems to me that Charles Dickens taught us (and Ebenezer Scrooge) a fundamental lesson: mankind is our business.

Paul Battaglia
Herndon, Virginia

ONLINE ARTICLES

The following correspondence refers to articles published only online

Tort lessons

SIR - The problem with George Bush's appetite for tort reform is that he pursues reform while pursuing deregulation just as zealously ("The war on tort", Global Agenda, Economist.com, January 26th). If both the monetary disincentive for wrongdoing and the regulations to guard against it are neutered simultaneously, the inevitable result will be great and unrecoverable damage to large numbers of consumers. A reduction in liability must proceed in combination with greater corporate regulation, not less. Otherwise, the resulting boon to business will come at a grotesquely unfair cost to consumers.

Thomas Walker
North Attleboro, Massachusetts

SIR - You are right that the tort system has gone askew in a few areas but you ignore the

substantial benefits to Americans as a result of the country's active body of trial lawyers. You might have noted the role that trial lawyers have played in the fight for civil rights, product safety or corporate accountability. Instead, you portray them as parasites with little to offer but campaign contributions to Democrats. Is it any wonder that "trial lawyers do not rank highly in the public's perception"?

Kyle Mach
Seattle

SIR - You mention spiralling medical-malpractice costs. A brief published by the Congressional Budget Office in January 2004 investigated the potential outcome of legislation to cap claims. Research of states that have already instituted caps found that they did result in reductions in claims paid of up to 30%, but since medical-malpractice claims account for only 2% of total medical costs, the net result would probably lower health-care costs by 0.5%. The CBO also compared health-care spending per head between states with lawsuit caps and those without and found no significant difference. Tort-reform legislation may temporarily gratify Congress's need to solve all of America's problems but it will provide little change in health-care costs.

Brad Wilks
Wexford, Pennsylvania

SIR - To keep corporations accountable, nothing stirs the conscience quite like hefty damages awarded. Ultimately, the decision for tort reform will depend on what we value more: low prices with the possibility of endangerment or high prices with very cautious practitioners.

Elizabeth Napp
Mount Kisco, New York

Voting in Iraq

SIR - In "Defying the Bombers" (Global Agenda, Economist.com, January 31st) you wrote: "...astonishingly, a modest stream of voters was seen in the bombed-out remains of Fallujah." Why is that astonishing? It is surely because of the fact that the anti-democratic terrorists were cleared from Fallujah late last year that people were actually able to vote with a higher degree of confidence in their security than they would have had otherwise.

Mitch Mitchell
London

Emerging markets

SIR - With regard to your Buttonwood column on emerging-market debt ("The end of the affair?", Global Agenda, Economist.com, January 25th), there is of course an alternative explanation for the lower spreads that emerging-market bonds command over US Treasuries: investors may perhaps think that the risk involved in investing in securities of the United States, with its high fiscal deficits, denominated in dollars, has risen. This would result in Treasury yields converging with emerging-market debt yields.

Roy Adams

SIR - You question why American portfolio investment in emerging-market bonds has risen in the last few weeks. For small American investors, investing in international bond and equity funds is

one of the few relatively convenient ways we have of trying to protect ourselves from the looming threat of dollar devaluation. All of us who passed Econ 101 are scared stiff by the myopia of the Bush administration and insist on holding a fair percentage of our portfolio in assets that might rise when the dollar sinks: foreign stocks and bonds, energy, and American companies with relatively high foreign sales.

Ron Brandstetter
Milwaukie, Oregon

SIR - Your article on emerging markets incorrectly mistakes ABRA for GCAB (Global Committee of Argentina Bondholders). ABRA played no role in the "Not the Argentine Road Show".

Adam Lerrick

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SPECIAL
PRINTABLE PAGE VIEW SPONSORED BY

Thailand's election

Thaksin's way

Feb 3rd 2005 | BANGKOK
From The Economist print edition

AP

A formidable success story, though with some worrying signs

Get article background

THE most remarkable thing about Thailand's impending election is the timing. It takes place on February 6th, over four years since the last one. In other words, the outgoing government, led by Thaksin Shinawatra, a tycoon-turned-politician, has survived for a complete parliamentary term—a first for Thailand. In the decade before the last election, the country churned through eight different governments, including one installed by a military coup. Yet after four years as prime minister, Mr Thaksin is still going strong.

Thai Rak Thai, the party Mr Thaksin founded before the last election, will almost certainly win this one outright—another first. The last time round, it fell just short, with 248 out of 500 seats, and secured an absolute majority only by absorbing several smaller parties. Now Mr Thaksin is targeting as many as 400 seats. Analysts reckon that target may prove just a bit over-ambitious, but Thai Rak Thai's main rival, the Democrat Party, concedes that it cannot possibly win. It is asking voters only for enough seats to provide a credible parliamentary opposition. After decades of rickety coalitions, Thailand is quickly becoming a one-party state.

Thailand's economy has also changed beyond recognition since Mr Thaksin became prime minister. In 2001, the year he took office, the economy grew by a sclerotic 2.1%. Fallout from the Asian crisis of 1997 was still evident. Banks, weighed down by bad debt, were not making new loans. Businesses, many of them bankrupt or saddled with useless excess capacity, were not hiring or expanding. Those who still had jobs had reined in their spending for fear of losing them, while

those who had lost them returned to their native villages, leaving 14% of the population below the government's poverty line. Skeleton high-rises, abandoned in mid-construction, punctuated the Bangkok skyline.

Last year, by contrast, the economy grew by perhaps 6.2%, after spurting ahead by 6.8% in 2003—its best showing since 1995. Non-performing loans are down to just 12% of the total, from a high of almost 50%. Poverty has fallen to less than 10%. Many previously suspended construction projects are under way again. Traffic in Bangkok, a reliable economic indicator, is approaching gridlock once more, thanks to the record number of new cars that have taken to the roads in the last few years.

Mr Thaksin's supporters attribute his political ascendancy, and the economic growth that has accompanied it, to the prime minister's acumen. Opposition politicians, needless to say, see things differently. They claim that Mr Thaksin has manipulated the political system unfairly to consolidate his power. His economic achievements, they say, are transitory, and more in the interests of his family firm and other big businesses than of the nation as a whole. As Ammar Siamwalla, a prominent local economist, puts it, next week's vote is not so much an election as a referendum on Mr Thaksin. Although most Thais seem to believe that the prime minister's strengths outweigh his weaknesses, concerns about how, and in whose interests, he is running the country are likely to grow, along with his mandate.

CEO style

There is no doubting Mr Thaksin's political savvy. He adapted more nimbly than other politicians to Thailand's new constitution, adopted in 1997 in an attempt to provide more durable governments. It strengthened the prime minister's hand by banning politicians who switch parties within 90 days of an election from standing in it. Since the prime minister controls the timing of elections, Mr Thaksin has been able to recruit opposition MPs to Thai Rak Thai without worrying about this rule. But Thai Rak Thai members cannot defect, for fear that Mr Thaksin may call a snap election to punish them.

The constitution also introduced a new electoral system, which Mr Thaksin has proved adept at using. Voters opt not only for a candidate in their constituency, but also for a party. In parliament 100 seats are then distributed among the parties in proportion to their share of these “party list” votes. Parties used to concentrate on recruiting the strongest candidates, and neglected policy platforms, which tended to fall by the wayside during coalition negotiations in any case. But at the last election, Mr Thaksin laid out and promoted a clear agenda for Thai Rak Thai, in a bid to sweep the party list. His promises—of medical care for just 30 baht (75 cents) per consultation, debt relief for farmers and micro-credit for villagers—proved so popular that the other parties are now following suit. The Democrats, for example, are offering free health care, free education, pensions for the old, guaranteed jobs for university graduates and more debt relief. Thai Rak Thai, for its part, is promising voters all manner of goodies, from expanded public transport to free cows.

Such policies are just one example of Mr Thaksin's shrewd marketing tactics. Instead of relying exclusively on backroom deals to win office, he has attempted to sell himself directly to the voters. He likes to draw a contrast between the ups and downs of his career as an entrepreneur and the narrow experience of his electoral rivals, who are professional politicians and provincial power-brokers for the most part. As a phenomenally successful telecoms tycoon, he argues, he has both the managerial skill to run the country, and wealth enough to resist corruption.

There is no challenge Mr Thaksin will not take on: he has pledged to eliminate drugs, poverty and drought, to name but a few. He is constantly launching ambitious schemes, setting improbable deadlines, and sacking the hapless officials who do not meet them. Voters, used to short-lived and

tentative governments, adore this “CEO style”. Mr Thaksin's ratings soared, for example, after December's tsunami, when he rushed to the scene, berated officials for their incompetent response and ordered speedy remedies, always in view of a television camera.

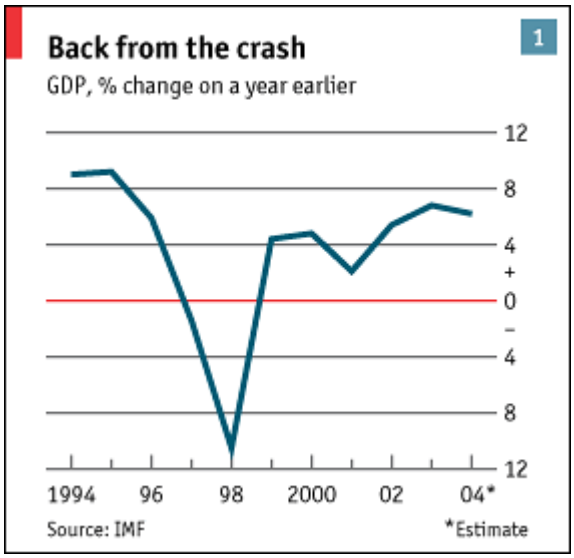
On the whole, these innovations have helped to make Thai politics more responsive to the concerns of ordinary voters, and less dependent on the whims of greedy machine politicians. But that does not mean, as some of Mr Thaksin's supporters argue, that he has nurtured democracy by doing away with Thailand's traditional “money politics”. After all, Mr Thaksin actively courts provincial barons. The Democrats claim to have a recording of Newin Chidchob, one of Thai Rak Thai's most recent recruits, offering big payouts to party canvassers and government officials who help secure their districts for Thai Rak Thai—a claim Mr Newin denies. Indeed, all the big parties continue to field candidates from provincial dynasties, often despite their unsavoury reputations, presumably because they still have plenty of clout.

Democratic difficulties

Moreover, Mr Thaksin does not seem too exercised about democratic niceties. He has complained about having to answer to unelected judges, and argued that restraints on his authority are unnecessary, since he has his wife to keep him in line. He has appointed his cousin supreme commander of the armed forces, and his brother-in-law assistant chief of the national police. During his tenure, Thailand's various watchdog agencies have lost much of their vigour and independence. The Senate has selected two former members of his staff to serve on the Constitutional Court. Other friends and associates have joined the National Counter Corruption Commission, which had previously accused Mr Thaksin of corruption.

The local media, too, has lost much of its vibrancy over the past four years. Shin Corporation, the Shinawatra family's holding company, has bought iTV, Thailand's only independent television channel, and sacked many of its reporters. The government and armed forces already own all the other stations. Editors complain that government agencies and Shin Corporation subsidiaries withhold advertising from newspapers critical of the prime minister. The family of Thai Rak Thai's secretary-general recently bought a big stake in the *Nation*, Thailand's most outspoken paper.

Mr Thaksin sometimes seems to lose sight altogether of the welfare of his lowliest compatriots. He refused to call off his “war on drugs”, even when it resulted in the deaths of over 2,000 alleged dealers, and despite the claims of human-rights activists that the police might have been involved. Mr Thaksin also refused to condemn the police when they quelled a demonstration of angry Muslim youths by shooting six of them, and packing the rest so tightly into police vans that 78 of them suffocated. In another incident, several Thais died of avian flu while Mr Thaksin's ministers denied that the disease existed in Thailand.

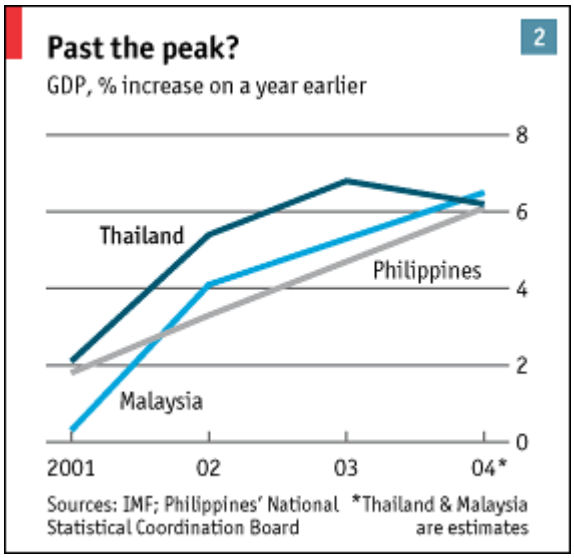


On the economic front, Mr Thaksin's record is somewhat ambiguous. The many forms of stimulus introduced by his government definitely helped to stoke Thailand's growth rate. In keeping with campaign pledges, he suspended farmers' debts, radically reduced the costs of government health care and set up micro-credit funds of 1m baht in every village in Thailand. He bought up the bad debts of state-owned banks so that they could resume lending, and then pressured them to do so. He subsidised the prices of housing, petrol and computers, among other things. Growth duly accelerated to levels not seen since the boom years of the 1990s (see chart 1).

Economists feared that this wholesale pump-priming, although effective in the short term, would end up bankrupting the government, or inflating a new bubble akin to the one that burst so disastrously in 1997. But public debt has actually fallen during Mr Thaksin's tenure, from 54% of GDP in 2000 to 39% now. Some doubt remains about the true extent of the government's liabilities, thanks to the many spending schemes that do not show up in the budget. Mr Thaksin's largesse has also fostered a culture of easy credit, one of the factors that contributed to the crisis of 1997. Krung Thai, the state-owned bank that accounted for the bulk of Thailand's loan growth in 2002 and 2003, recently announced a big jump in bad debts. But Supavud Saicheua, an economist at Phatra Securities, a local investment bank, estimates all off-budget liabilities at 8% of GDP at worst—a hefty figure, to be sure, but not enough to provoke fiscal meltdown.

Yet even if Thaksinomics has not fulfilled sceptics' fears, it has not lived up to its author's expectations either. Mr Thaksin wanted not only to stimulate the economy, but also to improve its long-term performance by reducing Thailand's dependence on exports. By providing what he called the “grass-roots economy” with capital and marketing expertise, he planned to create a new engine of growth. But the hoped-for transformation has not yet materialised. Today, exports account for 68% of national income, slightly more than when Mr Thaksin took office.

Nor have the prime minister's spending programmes clearly improved the lot of rural voters, with whom they are so popular. Rural incomes have risen, but largely as a result of higher prices for agricultural goods. In a study of the village-level micro-credit funds, Wichai Turongpun, of the National Institute of Development Administration, found that only 21% of money lent was invested productively. The rest went on consumption, or the refinancing of higher-interest loans. Moreover, villagers' expenditure appeared to be rising faster than their income, despite lower interest payments and access to subsidised health care. The poorest fifth owed an average of 68% of their annual income last year, compared with 60% in 2002. At some stage they will inevitably have to rein in their spending, or borrow more.



In short, says Thitinan Pongsudhirak, a professor at Chulalongkorn University, the government's grass-roots development schemes have provided a one-off boost to consumption, but will have little impact on growth in the long run. One theory holds that Mr Thaksin's policies simply advanced the country's economic cycle. After all, Thailand's economy peaked in 2003, while those of its neighbours continued to grow steadily (see chart 2).

Family affairs

The biggest weakness in Mr Thaksin's economic policy, however, is his failure to address the potential conflict of interest between his roles as prime minister and head of Thailand's wealthiest family. Mr Thaksin used to be Thailand's richest man, but transferred all his assets to relatives when he became prime minister, as required by law. That step, although important, does not prevent him from acting in his family's interests—and they are many. Either directly or through Shin Corporation, his relatives have stakes in Thailand's biggest mobile-phone company, its only commercial satellite operator, a bank, a television channel, an internet service provider, an advertising firm, an airline, a property developer and many similar investments in neighbouring countries. Nor is Mr Thaksin the only member of the cabinet with close connections to business. Other ministers belong to families that own, variously, an agribusiness and retailing conglomerate, a car-parts firm, and other telecoms and television companies.

Mr Thaksin and his colleagues strenuously deny that they have in any way favoured their family's firms, and have sued several journalists for suggesting as much. But in a recent book* two academics, Pasuk Phongpaichit and Chris Baker, point to several government decisions that appear, at any rate, to have benefited businesses connected to members of the cabinet. In 2001, the government decided to limit foreign holdings in telecoms companies to 25%, a level that would have affected other mobile firms, but not Shin Corporation's Advanced Info Services. In the face of concerted opposition, it reversed the decision. The same year, the Land Department validated Mr Thaksin's acquisition of a disputed property, overturning an earlier ruling by the Council of State. In 2003, the airport authority granted Thai Air Asia, an airline in which Shin Corporation has a 50% stake, a discount on airport fees.

The stockmarket valuation of most Shin Corporation firms has risen astronomically during Mr Thaksin's tenure, along with their profits. Brokers say firms connected to Mr Thaksin trade at a premium, although Shin Corporation argues that the higher valuation simply reflects better management. At the very least, Mr Thaksin's eagerness to stimulate domestic demand has proved

a boon for many firms in his family's stable.

Whatever the reason for Shin Corporation's success, the business interests of Mr Thaksin's family are so vast and varied that he must constantly be formulating policies that impinge on them, and thus laying himself open to accusations of impropriety. Yet Mr Thaksin's government has not adopted any formal system to guard against self-serving conduct. Ministers do not recuse themselves from decisions that might affect their family's businesses. Instead, Phongthep Thepkanjana, the justice minister, explains lamely, if anyone in the cabinet tried to promote a biased policy, his colleagues would shout him down.

Suranand Vejjajiva, a spokesman for Thai Rak Thai, notes that Mr Thaksin has complied with all legal requirements concerning conflict of interest. Furthermore, he argues, Mr Thaksin has tried to improve the transparency of Thai business by strengthening stockmarket regulation and banking supervision. He also points out that Mr Thaksin has initiated a war on corruption, although he admits that the results have been disappointing so far.

A man unopposed

None of these measures, however, addresses the central concern: that Mr Thaksin's connections to business are too close to allow truly disinterested policymaking. Such misgivings will only grow with a new Thaksin-led government. For a start, Mr Thaksin is likely to be in a stronger position in parliament. Only the Democrat Party offers vociferous opposition, and it is riven by internal disputes. The media is also more quiescent now, as are independent agencies such as the National Counter Corruption Commission. Nor do ordinary Thais seem much concerned, despite the best efforts of the Democrats to stir up their indignation.

Furthermore, Shin Corporation's business interests are constantly expanding. The purchase of its stake in Thai Air Asia, for example, took place after Mr Thaksin became prime minister. Panthongtae Shinawatra, the prime minister's son, has also recently gone into business. He is currently competing for an advertising concession on Bangkok's new subway system.

Indeed, Mr Thaksin's strengths and weaknesses as a leader are inextricably linked. His innovative ideas for reviving the economy derive, naturally enough, from his past life at the helm of Shin Corporation. It would be odd indeed if there were no convergence between his outlook and the firm's. By the same token, he has proved far more enduring and politically effective than most of his predecessors—but his effectiveness stems, in part, from discouraging dissent and undermining challenges to his authority. For Thais going to the polls this weekend, there is no unravelling the ecstasy and agony of voting for Mr Thaksin.

---

* “Thaksin: The Business of Politics in Thailand”. By Pasuk Phongpaichit and Chris Baker. Silkworm Books, Chiang Mai 2004.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

State of the union

The revolution, phase two

Feb 3rd 2005 | WASHINGTON, DC
From The Economist print edition

Reuters

The president is intent on spending his political capital quickly

STATE-of-the-union addresses set a tone as well as an agenda. The “axis of evil” address of 2002 did so for George Bush's first term. It was sombre, warlike, international. To judge by the latest address—Mr Bush's first since his re-election—the second term could be very different.

For the first time in a long while, the domestic agenda was more interesting than the foreign one. The first term saw the ascendancy of America's willingness to go it alone, the triumph of national interests broadly conceived. In this speech, Mr Bush promised both a more diplomatic America, one that stresses soft power, and a more idealistic one—a country that turns the rhetoric of his inaugural address about “ending tyranny” into policy. What both terms have in common, though, is Mr Bush's self-confidence in his ability to change his country and the world—and his willingness to gamble hugely.

Social Security was the centrepiece of the address. The speech was not—and was not expected to be—a blueprint for reforming the pensions system. Mr Bush did not espouse any particular plan, nor propose specific changes. Rather, he offered explanations, reassurances and options.

He called the pensions system “a great moral success of the 20th century” (ie, we don't want to change it just because we have hated the system on ideological grounds all along). But “on its current path, [it] is headed towards bankruptcy.” The system will be paying out more than it takes in by 2018, the president said (the Congressional Budget Office says 2020) and will be bankrupt by 2042. In an attempt to refute those who say this amounts to a long-term problem, but not a crisis, he put the case for acting now in household terms: 2018 is when your five-year-old would

go to university; 2042 close to when your 20-year-old would retire.

As a piece of salesmanship, this may well be effective. But to bolster public reassurance, Mr Bush argued that reform is not as risky as opponents claim. Those over 55 would not be affected—an attempt to appease the powerful old people's lobby (see article). Personal retirement accounts would be voluntary. People could divert up to four percentage points of their payroll taxes. And the changes would be phased in (administration officials propose to start the reform in 2009 for workers 44 years or older).

All this is politically astute, and necessary. His speech was less a policy statement than the opening move in a campaign to reshape a debate where public opinion is both sceptical and divided. This was the moment Mr Bush nailed his colours to the mast of Social Security reform.

The president has to take his case to the public because in Congress even his supporters are nervous. Republicans do not want to reform Social Security without some Democratic support. But the Democrats are almost unanimous in opposition. And because Mr Bush does not have enough support to dictate terms to Congress (as he did with tax cuts in the first term), he has had to let Congress choose the particular reform, hoping to attract more votes for change that way.

But it is not so clear whether the state-of-the-union address has advanced or reduced Congress's appetite for change. At a meeting in West Virginia the weekend before the address, congressional Republicans agreed to support the president's cause. They did so without much confidence he will succeed. Roy Blount, the Republican majority whip, said his members had gone from “cautious to being cautiously optimistic”. But he conceded the battle was taking place “way out there beyond our defences”.

As for the Democrats, their leader in the Senate, Harry Reid, claimed Social Security reform was dead. At least 40 of his colleagues in the Senate opposed it—enough to filibuster any proposal to death.

In attempting to change Democratic minds, Mr Bush listed a number of options for reform—increasing the retirement age, indexing benefits to prices not wages, changing the way benefits are calculated. All these are things that some Democrats have espoused in the past. Anything is negotiable, he implied.

But having opened up the possibility of negotiations, Mr Bush seemed to slam the door shut again. “We must, however, be guided by some basic principles,” he said: no increase in payroll taxes, and private accounts financed by diverting part of those taxes. Tom Mann of the Brookings Institution argues that the few Democrats who might possibly support some sort of change are more likely to be put off by these “basic principles” than encouraged.

In other words, the chances of Social Security reform hinge on Mr Bush's ability to change the political landscape to make Democratic opposition unsustainable. The day after the speech, he began a two-day trip to states with wavering Democratic senators. Taking his case directly to voters worked with his tax cuts. But in the first term Democrats were on the defensive about tax cuts, and loth to oppose them. Now, Republicans are on the defensive about Social Security and unwilling to attack it. Where the first term saw a succession of relatively bloodless presidential victories—partisan routs in the case of tax cuts, bipartisan agreements in the case of education reform—the second term will see a bloodier battle on Social Security, whoever wins.

Freedom abroad

The second term is likely to see significant changes in foreign policy, too, though the consequences are harder to foresee. In some ways, the state-of-the-union speech was strikingly “soft” and multilateralist.

Mr Bush basked in the glow of the Iraqi election. The hard cases of diplomacy were almost waved away. He mentioned North Korea only to say America was negotiating with Asian powers to dismantle its nuclear-weapons programme. He mentioned Iran's nuclear programme in the context of European-led diplomacy. He said a two-state solution to the Palestinian-Israeli conflict was “within reach”; promised $350m to support Palestinian reform; and dispatched Condoleezza Rice, his secretary of state, to the region. He even had nice words to say about the European Union and—gasp—the United Nations. In some ways, his speech confirmed the tilt from unilateralism that Ms Rice implied when she told the Senate that “the time for diplomacy is now.”

Yet the speech had a final, more intriguing component: unusually in a state-of-the-union address, Mr Bush urged two close allies, Saudi Arabia and Egypt, to “show the way toward democracy in the Middle East”. As Norm Ornstein of the American Enterprise Institute says, it was the kind of tough rhetoric that demands a response from the admonished—or they risk a more clamorous American follow-up. Mr Bush also seemed to encourage Iranians to rise up against their clerical regime by saying “as you stand for your own liberty, America stands with you.”

In other words, Mr Bush went out of his way to insist that the recent inaugural hymn of praise to liberty was not just windy aspiration, but a guide to foreign policy. It is hard to say which is the more ambitious aim—this or transforming America's largest and most popular domestic spending programme.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The AARP

Still the biggest bruiser?

Feb 3rd 2005 | WASHINGTON, DC
From The Economist print edition

A large grey blockage to the president's hopes

IF PENSIONS are the third rail of American politics, the AARP generates much of the lethal current. The American Association of Retired Persons, as Washington's most powerful lobbying group used to be called, hopes to destroy George Bush's plan to reform the Social Security system.

The AARP's opposition to diverting payroll taxes from Social Security into private accounts is as well known as the president's enthusiasm for "an ownership society". But the swiftness of its pre-emptive attack still came as a surprise. Even before the inauguration, the AARP had launched a $5m advertising campaign. "If we feel like gambling, we'll play the slots," say a sensible middle-aged couple in one print ad. A television blitz aimed at younger voters is coming next.

From Mr Bush's point of view, the AARP has a depressingly impressive record. Without its help, the hugely expensive bill to include prescription drugs in Medicare cover would never have squeaked through Congress in 2003. Although the AARP does not give a dime to any politician (and refuses to endorse them, even if attractively ancient), its imprint is on dozens of other laws affecting entitlement programmes.

Top of the heap
Membership of selected advocacy organisations

	Total, m
AARP	35.0
AFL-CIO	13.0
National Rifle Association	4.0
Sierra Club	0.7
National Association for the Advancement of Coloured People	0.5
National Organisation for Women	0.5

Sources: Organisations

The AARP's strength lies in its 35m members—far more than any other politically active group (see table). The old vote in higher numbers than the young do, and the AARP is better at rounding them up than anybody else. Wrinklies are wooed with discounts on insurance, motels and cruises; less elderly baby boomers are targeted with cheap AOL accounts. Changing its name to the snappier AARP in 1998 was also a boomer-marketing gesture.

The organisation sells its members health and life insurance, and ploughs the proceeds into its advocacy efforts. These vary from fighting age discrimination to helping the old with their taxes

and protecting them from dodgy bank loans. Still, it often feels like a business enterprise, with total revenues of $770m in 2003, plush offices and well paid managers.

Some critics suspect this is a source of weakness: that the AARP's footsoldiers see it as their insurance salesman, not their political leader. “I puzzle at just how strong the grassroots are in terms of policy,” says Joseph Antos of the American Enterprise Institute, a think-tank. “I'm certain they are strong in terms of discounts.” Others point out that the AARP is up against the most brutally effective White House in living memory, Wall Street and much of the conservative movement. Already champions of private accounts, such as Progress for America-Voter Fund and the Club for Growth, are gearing up for a counter-attack on behalf of reform.

However, as yet there are few signs of the AARP going soft. The February issue of its *Bulletin* features a (somewhat one-sided) article entitled “Why privatisation bombed in Britain”; it recounts the supposed folly of the Thatcherite reforms, which bore some similarity to the Bush proposals. The organisation has already released two notably hostile polls, one of which helpfully reminds Republican congressmen that “the more Americans learn about diverting Social Security taxes into private investment accounts, the less they like the idea.”

If anything, the AARP faces an easier job with Social Security than it did with the Medicare drug law. Some 60,000 members resigned then, cross about the paltriness of the drug benefit or worried about the AARP's potential conflicts of interest: the new law will allow the AARP to sell them prescription-drug plans from 2006. With pensions, the AARP will set itself up as the only organisation looking after the interests of old people—as opposed to the money-grabbing bankers from Wall Street and the ideological zealots of the right.

Is there any room for compromise? Bill Novelli, the AARP's avuncular boss, sounds reasonable enough: “We're meeting with everybody,” he insists. But his opposition to diverting payroll taxes into private accounts—or as he likes to call them, “carve-outs”—seems non-negotiable. That presents a big problem for the president.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Paedophilia cases

Claims, counter-claims

Feb 3rd 2005 | CAMBRIDGE, MASSACHUSETTS, AND LOS ANGELES
From The Economist print edition

A priest, a singer and the difficulties of proving cases of child abuse

IT IS hard to look at the Paul Shanley of today—a withered, balding man of 74 at a court defendant's table—and picture the swashbuckling priest he used to be. In the 1960s and 1970s, Mr Shanley was a dark-haired crusader in jeans who ran a “street ministry” for addicts and runaways in Boston, a courageous champion of gay rights against the church hierarchy. Was he also a predator who molested and raped dozens of vulnerable boys, in decades of abuse that the archdiocese of Boston covered up?

The trial of Mr Shanley, which was due to go to the jury just after *The Economist* went to press, has had a profound effect on Boston. It also amply illustrates the difficulties of bringing paedophilia cases—coincidentally, just as jury selection has begun in the highest profile paedophilia trial of all time, that of Michael Jackson in Santa Maria, California.

For critics of the Catholic church in Boston, Mr Shanley's trial represents a rare chance for one of the alleged abusers to be sent to prison. The archdiocese has paid out millions of dollars in civil-lawsuit settlements, some of it to alleged victims of Mr Shanley. But statutes of limitations, which limit criminal cases, in effect, to events that happened 15 or fewer years previously, have saved most of the accused men from facing criminal charges. The current case, relating to events in the 1980s, can be brought only because Mr Shanley moved away from Massachusetts in 1990, technically creating a gap in his residency in the state.

AP

The ordeal begins

The case hinges on the memories of one 27-year-old firefighter, who says he was six years old when Mr Shanley began to abuse him in a suburban Boston parish. The alleged victim, thick and muscular now, broke into sobs on the witness stand when he described repeated rapes in the boys' room and confessional, and a card game, called “War”, in which the loser had to remove a piece of clothing. He says he repressed memories of the molestation for nearly two decades, recalling them only after reading press reports about Mr Shanley three years ago.

Sexual abuse cases, which usually hinge on two peoples' memories of an alleged event, are notoriously (and rightly) hard to prove. In this case, Mr Shanley's defence team has torn into the accuser's version of events, pointing out inconsistencies in his story and also detailing his abuse of alcohol and steroids. Experts have been called to testify that repressed memories can be planted in a susceptible mind. The defence claims that the accuser, who won $500,000 in a civil settlement, is motivated by money: he had to claim that his memory had been repressed in order to file the civil suit, where the statute of limitations is two years.

Mr Jackson's trial has begun with considerably more hoopla, with the defendant shimmying into court in a white suit and jewelled vest to the cheers of his ardent fans. But it shares many of the same problems. If it was hard to find impartial jurors for Mr Shanley's case, it will be impossible to find anyone who does not already have some knowledge of Mr Jackson's. It also rests on the claims of a single alleged victim, who many outsiders (wrongly or rightly) feel represents other accusers: a single 15-year-old boy, a recovering cancer patient, says he was abused two years ago at Mr Jackson's “Neverland” ranch. The rock star says the boy is lying, and that his mother pressed the case for financial gain. Like the archdiocese, Mr Jackson has also reportedly paid money to his accusers—to settle a civil molestation case launched in 1993.

For Mr Shanley and Mr Jackson, both of whom have maintained their innocence, the stress is obviously enormous. But the trials are plainly not easy for the accusers either. Three other men, who were originally part of the Shanley case and who had also received civil settlements, dropped out—one of them after an aggressive grilling by the defence team at a pre-trial hearing. The lone remaining fireman is clearly feeling the burden. After a gruelling cross-examination, he begged the judge not to call him back the next day. “Please don't make me,” he said. “I can't do this again.”

Prosecutors insist that the man's willingness to testify is proof that his motives are pure. The jurors, who are barred from hearing many details of Mr Shanley's past, will weigh that against the testimony of those memory experts and the image of a slender old man with a hearing aid.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Great American sports

You're chicken

Feb 3rd 2005 | WASHINGTON, DC
From The Economist print edition

That little red rooster's got gloves on

COCKFIGHTING was banned in Oklahoma after a referendum in 2002. Now a plucky state senator has proposed a bill to bring it back, albeit with a few crucial changes. Frank Shurden wants the cocks to wear tiny foam-filled muffs on their spurs and protective sparring vests while they duke it out.

Mr Shurden admits he has only seen a brochure for the equipment, patented by a Californian lawyer, but he predicts “gamecock boxing” will be a boon to tourism and state coffers. He hopes the new sport will be adopted by the horse-racing industry and staged between races at the track. That way, gambling on the fights will be legal and taxable.

By taking the blood out of the sport, Mr Shurden hopes to blunt the opposition of animal-rights groups. In proper cockfights, which are still legal in New Mexico and Louisiana, roosters are fitted with knives or gaffs on their spurs and often fight to the death. Senator Shurden compares gamecock boxing to “fencing in the Olympics”. Electronic sensors on the sparring vests will record the hits scored, and the clucking pugilists will fight rounds “just like people do”.

Animal-rights activists are not convinced. “Even if fitted with muffs, these roosters will deliver blows that will knock out eyes, break bones and possibly even kill,” says Cynthia Armstrong of the Oklahoma Coalition Against Cockfighting. Mr Shurden admits there could be some face-pecking, but insists the sport would not violate the chickens' rights: “We're just letting them do what comes natural to them.” Odd words, perhaps, from a long-time champion of castration for sex offenders.

Mr Shurden also faces practical problems. For instance, Oklahoma's cockfighting ban after the 2002 vote also made training fights, in which muffs are used, a felony. Meanwhile, his roosters-in-slippers version of cockfighting may be a little tame for the state's cockfighting lobby. Unabashed, Mr Shurden is planning to stage a demonstration in the statehouse. “We'll get 'em down in the rotunda and let 'em fight.”

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

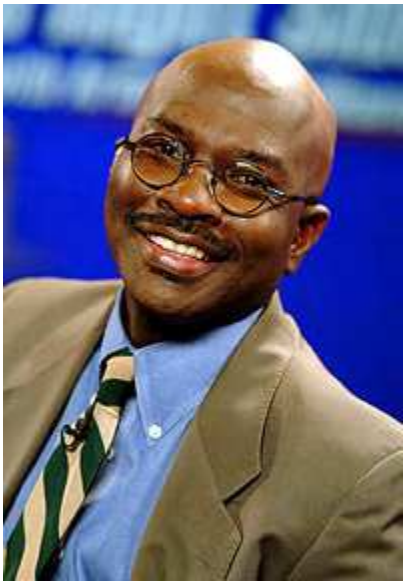
Journalists, politicians and ethics

Fourth estate or fifth column?

Feb 3rd 2005 | WASHINGTON, DC
From The Economist print edition

The perils of using journalists as propagandists

AP



Pundit Armstrong

MOST policy issues are genuinely tough. But just occasionally, something comes along that is as straightforward as it looks. Is it a good idea for a government to look as if it is paying bribes to journalists? Or for a government to put out fake news reports? No and no. And George Bush, at least, gets it. “I expect my cabinet secretaries to make sure that practice doesn't go forward,” he says. “There needs to be a nice, independent relationship between the White House and the press.”

Yet the past month has brought a slew of stories of government departments stomping all over that bright line. The most recent is the case of Michael McManus, a syndicated columnist. He got $10,000 from the Department of Health and Human Services (HHS) for helping train marriage counsellors. Before that it was Maggie Gallagher, another syndicated columnist: $21,500 from HHS for helping draft brochures promoting marriage. Before that came the biggest pay-off so far: $241,000 from the Department of Education to a talk-show host called Armstrong Williams to help promote Mr Bush's No Child Left Behind Act.

What were they thinking—paymasters and recipients? Well, HHS says Mr McManus was paid for his undoubted expertise, not for the many nice comments in his weekly column (and he points out he does sometimes chide Mr Bush there). Ms Gallagher got the money in 2002 while working as a researcher on marriage. She admits she should have disclosed the payments when she wrote about the issue later. Mr Williams got his cash from Ketchum, a public relations firm that has a $1m contract with the Education Department. He produced segments featuring the then education secretary, Rod Paige, which ran on his show as paid advertisements.

A host of investigations have started. The Federal Communications Commission is looking into whether Mr Williams broke the law. Congress's watch-dog, the General Accounting Office (GAO) is looking into the legality of the Education Department's actions. Rosa DeLauro, a Democratic congresswoman, has introduced a bill limiting government public-relations work, increasing oversight and banning publicly financed communication for partisan ends.

All three cases raise ethical questions for both journalists and politicians. For the scribblers, the most obvious problem is deceit. Journalists who do not disclose their financial interests are open to the charge of perpetrating a fraud on the public, since they are pretending to be impartial. This would be wrong even if they agree with the policies they advocate, and even if (as in two of the cases), they were paid money to work as researchers, not journalists.

In this respect, political journalists are in a position similar to financial reporters, who are usually banned from having any interests in companies they cover. Tribune Media has duly stopped distributing Mr Williams's column. Ketchum conceded that its contract with Mr Williams did not meet either its own ethical standards or those of the Public Relations Society of America, a professional body.

But the government faces different challenges from those facing private companies. Its actions in these cases were in some ways worse because it was acting on behalf of the nation. Public money was involved—and so are various laws restricting the use of public money to influence Congress or government policy. One says that taxpayers' dollars may not be used to pay a “publicity expert” unless specifically authorised for that purpose. Another forbids financing “covert propaganda”.

The GAO found that, in two previous examples, the Bush administration had fallen foul of these laws. In both cases departments or agencies created fake news footage, to be slotted into local news broadcasts, with actors playing reporters and “suggested introductions” for (real) anchors to read. One touted proposals for Medicare reform, another warned of the dangers of drug use. Whatever the legality of the new cases, the administration has muddied the relationship between government and press. (The Clinton administration issued fake news too, though those cases were not referred to the GAO.)

The abuses are the most obvious distortions produced by three growing trends which will surely produce more problems in the future. The first is the government's willingness to use public communications in new ways. In the past, public information was mostly about advertising eligibility for assistance programmes or for public-health announcements. The Education Department justified its contract with Mr Williams as part of a “minority outreach campaign” (Mr Williams's audience was largely black and Hispanic). But it is not clear that the No Child Left Behind Act is an assistance programme of the sort that needs advertising. And as the anti-drug and marriage initiatives show, the distinction between public-health information and social policy is eroding. Hence the administration stands accused of using public money to promote its policy interests.

Next, the government has sought to improve its operations by using private expertise. Over the past four years, according to a report by the minority staff of the House Committee on Government Reform, the federal government has increased the value of contracts with large public-relations firms from $37m in 2001 to $88m last year. Some of this work is unexceptionable: the Defence Department, for example, pays a PR firm to help with recruitment. But not all of it is. And PR firms use private codes of conduct that may not work for public business.

Third, the old boundaries between reporting, commentary and punditry are disappearing. Asked whether he had broken any journalistic code of ethics, Mr Williams replied “I'm not a journalist; I'm a pundit.” With more people seeking news from obviously partisan sources, and the notion of impartiality under attack, both government and individuals have a larger incentive to take advantage of residual good faith in journalistic impartiality.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Transport policy

The Windy City winds down

Feb 3rd 2005 | CHICAGO
From The Economist print edition

Corbis

Is the nation's transport hub grinding to a halt?

FROM his office, Earl Wacker can see the trails of aircraft flying towards O'Hare International, one of the world's busiest airports. But Mr Wacker's sights are focused on the gritty railway yard below his office window. As director of the Chicago Transportation Co-ordination Office (CTCO), he wants to improve an overburdened system that handles one-third of America's rail traffic. At present, a freight train trying to get across Chicago has to deal with up to four railroads: it can take days to get it across town.

If you are still waiting for your Christmas present, it may be somewhere close to the Windy City. Six of America's seven long-distance railroads meet there: add in local and regional services, and about 1,200 trains a day pass through the city. In addition to O'Hare, it also has a mid-sized airport at Midway. Seven interstate highways come through the region, and trucks move $572 billion in goods to, from and through it each year.

But is this hub working? The evidence in terms of congested roads and late trains and aircraft is not good. Road congestion alone supposedly costs businesses and commuters $4 billion a year. And the city's problems are expected to get much worse.

Air-freight tonnage in Chicago is projected to double in the next 25 years; the number of lorries coming through the area is expected to rise by 80%; rail volume should almost double in two decades. And there will be a compounding effect from the fast growth of inter-modal transport (switching freight from one “mode” to another, such as train to truck or aircraft) which tends to send even more traffic to hubs like Chicago. Even if the various growth forecasts prove to be only half true, they will tax the city's old infrastructure.

The ripple effects from the blockages around Lake Michigan are already felt across America. The rail traffic passing through Chicago eventually affects 5m jobs across the country, $780 billion in goods and $217 billion in wages. California, Ohio and New Jersey are the three other states most affected by rail bottlenecks in Illinois. Last month Union Pacific, the nation's largest railroad, said more carriers might be tempted to bypass Chicago. Canadian National and Burlington Northern Santa Fe have diverted some traffic through Memphis and New Orleans.

Last November, in a deal brokered by the Bush administration, domestic airlines at O'Hare, including United and American (which both use it as a hub), voluntarily limited their flights into the airport. A plan to expand O'Hare's runways is also moving forward in fits and starts. Some are still pushing for a third Chicago-area airport in Peotone, in the south suburbs. And the real dreamers talk about linking the airport into a European-style high-speed rail network that would reach other airports and cities across the mid-west.

Today the railways are in worse shape than the airports. Unlike the airlines, railroads don't have an oversight agency to co-ordinate their traffic: each of them uses its own dispatchers, who sometimes send faxes to their counterparts to let them know trains are coming. Mr Wacker's CTCO is a step forward in terms of co-ordination. But a much more ambitious $1.5 billion public-private plan—the Chicago Region Environmental and Transportation Efficiency (CREATE) programme—is awaiting federal funding.

CREATE involves plenty of sensible though expensive things, such as separating passenger- and freight-train crossings with rail-on-rail “flyovers”, adding rail connections to speed train traffic, and reducing the points at which trains and road traffic meet. The railroads have committed $212m towards it; the city and state have chipped in additional funds. But the bulk has to come from Congress, which has still failed to pass a transport bill.

As Robert Gallamore, a transport expert at Northwestern University's Kellogg School of Management, points out, the odds are in favour of CREATE getting its money. It has the support of Dennis Hastert, the House Republican speaker, whose district includes Chicago's western suburbs. Barack Obama, the new Democratic senator from Illinois, is on the Senate's public works committee.

A different solution

But even CREATE is unlikely to solve Chicago's problems. New roads will still be needed and, in a metropolitan area with 272 municipalities, it is hard to get locals to pay up. In the end, most of the long-term solutions involve forcing Americans to pay for the full cost of using their roads, airports and railways.

Last year Illinois's governor, Rod Blagojevich, inched that way when he unveiled a plan that charges lorries more for using highways in peak times. The decision by Chicago's mayor, Richard Daley, to lease the Chicago Skyway, a toll road into the city, to a Spanish-Australian consortium is “a sign of things to come”, says Frank Beal, the executive director of Metropolis 2020, a local policy group. The consortium has just coughed up $1.8 billion, beginning its 99-year lease. Private investment may be the only way to unblock America's hub.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Lexington

The odd couple

Feb 3rd 2005
From The Economist print edition

George Bush is having an intellectual love affair

“INTELLECTUAL” is hardly the first word that springs to mind when you contemplate George Bush. Mr Bush glided through the best education that money can buy without acquiring much in the way of “book learning”. At school, he formed a stick-ball team called the Nads (providing him and his pals with a chance to shout “Go Nads”); at Yale, he was famous for doing the alligator, a dance that involved falling on the floor and rolling around; at Harvard Business School, he wore cowboy boots and chewed tobacco, a strutting provocation to the lefty penseurs who dominated Harvard Yard.

Yet for the past few months this paragon of good ol' boy common sense has been infatuated with a book about an abstract noun by a Jewish intellectual. Mr Bush recommends Natan Sharansky's “The Case for Democracy: The Power of Freedom to Overcome Tyranny and Terror” (Public Affairs) to almost everyone he meets (including Condoleezza Rice, who mentioned the book during her opening remarks at her Senate confirmation hearing). Nine days after winning re-election he spent over an hour discussing the book in the White House with Mr Sharansky himself. The meeting must have sounded extraordinary, given Mr Sharansky's thick Russian accent and Mr Bush's Texan drawl. But by all accounts they got on famously.

Why is Mr Bush so infatuated with Mr Sharansky? Certainly not out of a desire to restore his favour with America's erstwhile allies. Mr Sharansky, a minister without portfolio in Ariel Sharon's Likud government, has a growing penchant for siding with the hard right. In two recent incidents he rallied with Jewish settlers to oppose Mr Sharon's plan for withdrawing from Gaza and criticised

the recent Palestinian elections for not being “truly free”. It is hard to think of anybody who is more likely to set off alarm bells in the chancelleries of Old Europe.

Mr Bush loves “The Case for Democracy” for the simple reason that he likes what it has to say. “I want you to read a book,” he told John Dickerson of *Time* magazine. “It will give you a sense of what I'm talking about.” Conspiracy theorists, not least in Israel, are already tracing the way that the evil Likudniks spread their influence. (A clue: Mr Sharansky ran into Dick Cheney at an American Enterprise Institute retreat in Beaver Creek, Colorado in June 2002, and had a long conversation with him. A few days later Mr Bush gave a speech telling the Palestinians that they needed to embrace democracy.) But this is less a case of presidential manipulation than of two minds thinking alike. Mr Sharansky is not so much Mr Bush's guru as his voice.

Mr Sharansky's message comes down to three points. First, “realpolitik” is bankrupt. America cannot go on coddling tyrannical regimes like Saudi Arabia because those regimes invariably try to buy stability at home by exporting hatred abroad. Second, democracy is the best insurance against aggression. Third, the world really is divided between good and evil.

There are few things that irritate foreign-policy types more about Mr Bush than his Manichean view of the world. His infatuation with Mr Sharansky suggests that he is not likely to be any more “sophisticated” in his second term. Mr Sharansky not only sees the world in black and white terms—good versus evil and free societies versus “fear societies”, with a bunch of “realists” dithering in the middle. He has also earned a right to such Manicheanism during his heroic years as a Soviet dissident.

Do as you say, Natan and George

The Bush-Sharansky “freedom doctrine” has come under heavy fire since Mr Bush's inaugural address (several passages in the address echoed the book almost word for word). In most cases, the criticisms say more about the critics. For instance, the Michael Moore crowd claim that Mr Bush doesn't really believe any of this claptrap about democracy—a charge that seems absurd, given the blood and treasure America has spent bringing elections to Afghanistan and Iraq. Meanwhile, a growing army of nouveaux Kissingerians mutter that democracy is not really that important. That is a hard charge to sustain after last Sunday's vote in Iraq. Still others worry that Mr Bush is selective in his targets, picking on Iran but not North Korea. Yet isn't politics the language of priorities? The fact that you can't do something everywhere is no reason to stop trying it somewhere.

There are nevertheless two substantial criticisms that can be made against the Bush doctrine, criticisms all the more telling for Mr Sharansky's presence on the freedom ticket. The first is that democracy is unlikely to promote peace if it is coupled with a burning sense of unresolved injustice. For Mr Sharansky, Palestinian rage is something that is artificially created by Palestinian and Arab elites as a way of keeping themselves in power. So turning Palestinians into democrats is a necessary first step to turning them into peacemakers. But Palestinian rage is also surely rooted in a sense that they have had their country stolen from them (not least by Mr Sharansky's settler friends). Democracy may simply give them another mechanism for expressing that rage: hence Hamas's success in municipal elections. If Mr Bush is serious about tackling the Middle East, he should choose a mouthpiece who is a bit less partisan.

The second is that you cannot spread goodness around the world unless you hold yourself to the same standards. Mr Sharansky has lost some of his moral authority because of his relative silence on the sufferings of the Palestinians—and not just among pampered Europeans but also among fellow Israelis, who know what it means to live in a tough neighbourhood. When Mr Bush talks about freeing captives, the rest of the world looks at Guantánamo Bay.

The trouble with Mr Bush's new doctrine is not that he has naively embraced freedom and democracy, but that he hasn't embraced them tightly enough.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Mining in Peru

Halting the rush against gold

Feb 3rd 2005 | CAJAMARCA
From The Economist print edition

Denver Post

Big mining and its increasingly radical opponents

Get article background

A PLEASANT town in a broad green valley in northern Peru, Cajamarca is the site of one of history's great betrayals. Some 200 yards from the main square, through a Spanish colonial doorway, stands a stone building known as the “Ransom Room”. Though this particular building may in fact have been his prison, in 1532 Atahualpa, the Inca ruler, offered to fill such a room with gold artefacts in order to win freedom from his *conquistador* captors. He kept his side of the bargain—but was murdered anyway. Now, once again, some people in Cajamarca complain that Peru's gold is being carried off by foreigners—and they are trying to stop it.

Astride the Andean watershed an hour north of Cajamarca is Yanacocha, one of the world's biggest and most profitable gold mines. Run by Newmont, a Denver-based company which owns it with Peru's Buenaventura, Yanacocha is a world away from the dark and dangerous gold mines of the past. At five separate sites, giant scoops slice the sides from mountains, loading 300,000 tonnes of rock a day into 250-tonne trucks, each the height of a four-storey building. The rock is laid out in terraces, sealed in black plastic, and injected with cyanide solution. This process yields an ounce of gold from each tonne of rock. So successful has Yanacocha been that its output has soared from 81,000 ounces of gold in 1993 to 3m ounces last year.

This headlong expansion has injected wealth into Cajamarca, though it is still one of Peru's poorest departments. The mine has produced fears and resentment too. For a fortnight last September, thousands of protesters blocked the road to the mine; supplies and staff had to be ferried to and

fro by helicopter. The protest was against Newmont's decision to prospect on Cerro Quilish, a mountain which locals say feeds streams that supply the city with drinking water. The protesters won hands down. Humbled, Yanacocha agreed to stop prospecting, asked the government to revoke its licence to do so, and issued an unprecedented public apology.

Two months later, at La Zanja, a six-hour journey from Cajamarca, a mob of some 350 locals, stirred up by extreme leftists, burnt and sacked a prospecting camp run by Buenaventura; they destroyed ten years' worth of rock samples. In December, three provinces in the area were shut down by a two-day protest strike against mining, while at Rio Blanco, close to Peru's border with Ecuador, a local-radio reporter was kidnapped by opponents of another proposed mine.

These events are widely seen as a turning point for mining in Peru—in more ways than one. “The pace at which we've expanded will be difficult to maintain,” admits Brant Hinze, an American who is Yanacocha's general manager. The protests also pose some broader questions. Will Peru remain one of the world's top mining countries? Will an alliance of local activists and rich-world NGOs thwart investment in a crucial industry? Or will both sides work together to ensure that mining is compatible with the environment and social development? The riot at La Zanja prompted several NGOs to issue a statement condemning violence. The government has sent police reinforcements to mining areas. “The state has drawn a line...[the threat to mining] is being seen as being as serious as drug-trafficking and terrorism,” says José Miguel Morales of the National Mining Society, who is also Buenaventura's general counsel.

The protests typically mix genuine grievance with ignorant fears that are whipped up by political extremists. In part, they are a sign of a more vigorous, if chaotic, democracy. They also reflect a mining boom. Although Peru has been a mining country since pre-Inca times, since 1992 output has tripled. In the decade to 2003, foreign mining companies invested some $6.7 billion in the country. Projects involving potential investment of more than $10 billion—and many of the world's top mining firms—are being explored.

While mining provides relatively few jobs, it is vital to Peru's economy in other ways. Thanks both to high mineral prices and rising output, mineral exports were up by almost half last year, and accounted for 55% of total exports. Mining brings in 29% of total tax revenues. Of this money, the government last year returned $138m as a local royalty to mining areas, most of which are otherwise poor and remote.

Because of its scale and prominence, Yanacocha may hold the key to mining's future in Peru. “If Yanacocha does things better, it will open the door to all mining projects in the north of Peru. If it doesn't, it will close the door to these projects,” says Marco Arana, a Catholic priest who led the protests over Cerro Quilish. The mine's critics focus on two things: its environmental impact, and its alleged lack of benefits for local people, many of whom are poor farmers.

Many of the environmental complaints, such as claims that the mine has polluted Cajamarca's drinking water with cyanide or mercury, look specious. An independent report by Stratus, a Colorado consultancy, found that while the mine's operations have “altered water quality and quantity in some locations and at some times” they have posed no threat to human health nor to drinking water. But the mine's rapid expansion has affected farmers. Several irrigation channels have dried up, while extra sediment in rivers has killed trout. Yanacocha has dealt with some of these complaints: it is spending $30m on three large dams to filter run-off water. In 2000, a contractor's truck carrying mercury from the mine had an accident; dozens of people in Choropampa, a nearby village, were taken ill. The mine spent $16m on cleaning up and compensation and has tightened procedures for the transport of dangerous materials.

It is hard to gainsay the mine's economic impact. Its 8,000 workers are well paid by local standards; another 40,000 jobs depend on the mine. Under pressure, Yanacocha is increasing the amount of supplies and services it buys locally. Cajamarca has the air of a boom town, with big new houses going up—along with brothels and noisy night clubs. In 2003, some $70m of Yanacocha's tax payments returned to Cajamarca as local royalty—a huge sum for a town of some 150,000. In addition, the company spent $14m on local social programmes, such as donations to schools and a regional hospital.

Scratch deeper, and other things lie behind the discontent. One is history: for centuries, mining companies (some of them state-owned) dumped toxic residues freely in Peru's fields and rivers. Since 1992, they have faced tighter environmental rules. The industry has spent $1 billion on cleaning up. But past pollution—and accidents such as at Choropampa—make farmers scared of new mines and of prospectors. And mines—like many farmers—do not pay for the water they use.

Second is Yanacocha's sheer scale: economically and politically, it dominates the city of Cajamarca. That generates great expectations and, since many in the area remain poor, envy and frustration. Some farmers sold their land cheaply to the mine and have watched land prices soar. “Yanacocha asks why they are seen as able to solve all the community's problems. It's because they've given that image...they use social investment as a means of social control,” says Father Arana.

Mr Hinze concedes that rapid expansion “caused us to overlook details”. He has told his managers to make greater efforts to listen to the communities around the mine. But he also points out that his company must strike a difficult balance: “it's our responsibility to return to communities some of the wealth”. But, he adds, “if you're not careful you become the government. We shouldn't become it.”

Indeed so. At the root of many of the conflicts over mining lies the weakness of the Peruvian state. If there is still much poverty in mining areas, that is not mainly the fault of the industry. Local governments are often corrupt and spend their mining riches badly. The corruption of the authoritarian regime of Alberto Fujimori, which ran the country from 1990 to 2000, robbed environmental regulation of credibility. Alejandro Toledo, the unpopular current president, has lacked authority and has struggled to keep order. In some places, says Dante Vera, a former interior ministry official now advising Yanacocha, protests are being whipped up by drug traffickers, former guerrillas and other extreme leftists. He worries that mining's expansion and

the radicalisation of its opponents could lead to violence.

Yet there are some hopeful signs. In December, after three years of talks, the managers of Tintaya, a copper mine run by BHP Billiton, signed a wide-ranging agreement with local communities backed by NGOs. Environmental and social responsibility have become part of the price of operating a mine in Peru. With prices high, that is fine. If and when they drop, the country may face some hard choices. For Peru cannot afford to do without mining.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The World Social Forum

Utopia, meet reality

Feb 3rd 2005 | PORTO ALEGRE
From The Economist print edition

An argument between reform and revolution

Reuters

It takes one to know one

THE last time tens of thousands of anti-globalisation activists gathered in Porto Alegre in southern Brazil under the banner of the World Social Forum (WSF), George Bush had yet to invade Iraq and Luiz Inácio Lula da Silva, then freshly inaugurated as Brazil's president, looked like the movement's entrée to political power in a big country. Now those who dream that "another world is possible" have sobered up. Iraq was invaded, and Lula's orthodox economic policies (see article) owe more to this world than to the next one.

Lula retains much of his popularity: cheers prevailed over boos when he spoke to the Forum on January 27th, and not only because his Workers' Party (PT) packed the stadium. But Lula then jetted off to Davos, a fat-cat gathering the WSF was set up to oppose. The real hero seemed to be a leader untainted by realism, Venezuela's leftist president, Hugo Chávez, who arrived three days later.

Lula's compromises have sharpened the division between those who think the current order can be fixed and those who insist it must be overthrown. As proof that progressives can change the system, he points to Brazil's leadership of the G20, a club of developing countries that fights to open rich-country markets through the World Trade Organisation. Many *forumistas* would agree with Diane Matte, a feminist from Canada, that "being at the table is being part of the monster". Some want to transform the Forum from a talking shop into a more unified political movement. Most of its leaders are resisting. It is a town meeting, they say, not an army or party.

This year's edition was bigger (it attracted 150,000 people) and, the organisers claimed, better. They let grass-roots groups decide what events to hold. These took place in dozens of sweltering tents strewn along the Guaíba River and dealt with everything from the virtues of indigenous culture to the evils of water privatisation. The Forum issued its own currency, the txai, but it could not buy anything really necessary, like mineral water. Now there will be a break from routine. Next year's Forum will be split into regional events—the Latin American version may be in Venezuela. In 2007 the activists will regroup, this time in Africa.

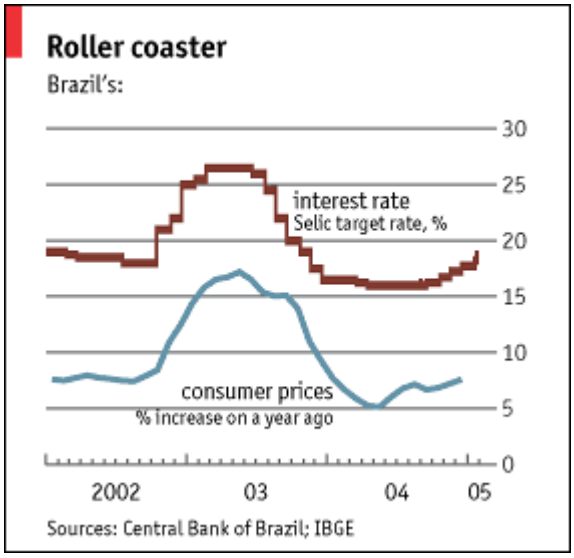
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Brazil's central bank

Risks, new and old

Feb 3rd 2005 | SÃO PAULO
From The Economist print edition

Is monetary policy too tough for its own good?



LAST year Brazil's economy turned in its best performance for a decade. Growth topped 5%, powered at first by exports but with investment and consumption joining in. The economy looks more resilient too: public debt fell to 52% of GDP in 2004 from 57% the year before. All this comes as a great relief for the president, Luiz Inácio Lula da Silva. He attracted much opprobrium, especially from parts of his own Workers' Party (PT), for backing the tough monetary policy of Henrique Meirelles, his steely central-bank chief, and the cautious fiscal stance of Antonio Palocci, the finance minister. But these stern policies paved the way for recovery.

It is odd, then, that Mr Meirelles is the target of a fresh bout of moaning from businessmen and politicians. Since September, the central bank has again been raising its benchmark interest rate to suppress an uptick in inflation. Last week the bank's monetary-policy committee hinted that it might tighten even further. Now, even his supporters wonder whether Mr Meirelles is overdoing it.

The bank's worry is that, untamed, inflation could in time kill recovery. It has fallen from 12.5% in 2002 to 7.6% last year—within the bank's target range. But Mr Meirelles has promised to push it down to 5.1% in 2005, and that will not be easy. He must contend with high world prices for everything from oil to steel, and sharp increases in utility tariffs. Factories and transport networks are operating at close to capacity. The result: the consumer-price index rose by a higher-than-expected 0.86% in December. Financial analysts' forecasts for inflation this year have edged down, but not yet to 5.1%. If necessary, says the central bank, it will step up “the rhythm and magnitude” of interest-rate increases.

The central bank is used to being blasted, even for the idea of inflation-targeting itself. Its friends worry not that it is misguided, but that it may now become over-zealous. “I would not like to see significant hikes ahead,” says Alexandre Bassoli of HSBC, a commercial bank. Already, it is clear that growth will slow this year. Export growth may weaken, in part because higher interest rates have pushed up the *real*, the currency. The rate hikes since September will be fully felt only after Easter. Investment is healthy, which should help keep a lid on inflation. Most economists expect the economy to grow by 3½-4%. But some fear a sharper slowdown—if the central bank over-tightens or if foreign demand slumps for Brazilian exports and bonds.

The central bank's next moves could be crucial for its future. It is plagued by rumours that Mr da Silva will sack hardline directors. This forces it to be even tougher than it might want to be in controlling inflationary expectations. The finance ministry therefore wants to give the bank formal autonomy, which Congress must approve. But that will not happen if the bank's toughness aborts the recovery. The risk of miscalculation has risen because the bank's mission has changed. In the past, it mainly grappled with the exchange rate and the impact of outside events. Now, says Monica Baer of MB Associados, a consultancy, it is “learning how to deal with interest rates related to the local market.”

Such risks have produced what looks like a new consensus: the central bank should accept a bit more inflation this year—say 5½-6%—rather than aiming to hit the target precisely. The cost to the bank's credibility would “not [be] overwhelming,” says Ilan Goldfajn, a former central-bank director now at the Catholic University of Rio de Janeiro. President Lula will not say so, but he probably hopes Mr Meirelles is listening.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Political succession in Jamaica

Moving on

Feb 3rd 2005 | PORT OF SPAIN
From The Economist print edition

Exeunt, without much glory

THE island has hardly been a success story in recent decades, yet Jamaica has shown remarkable loyalty to its political leaders. Percival (“PJ”) Patterson, the prime minister, has been in office since 1992. Edward Seaga, the leader of the opposition Jamaica Labour Party since 1974, has been around for even longer. He was appointed to the legislative council in 1959, the year that Fidel Castro entered Havana; he first won his West Kingston seat and a cabinet job three years later. Now, finally, both men are moving on.

Mr Seaga was persistently unsuccessful. He led his party to victory in only one contested election, in 1980; he won a second time by default, when the People's National Party (PNP), Mr Patterson's lot, boycotted a snap poll held in the wake of the American invasion of Grenada in 1983. Energetic slum clearance and background gun battles turned his marginal constituency into a personal fief. But since 1989, four successive PNP victories glued Mr Seaga to the opposition benches. Last month, he finally gave up: he has moved to the University of the West Indies. In his farewell address to the legislature, he lamented Jamaica's lack of progress in more than 40 years—something for which he must bear some responsibility. His successor, to be anointed at a party conference this month, looks certain to be Bruce Golding. He is hardly a new face, having left the party ten years ago over his impatience to become its leader.

Mr Patterson, too, has said that he will not fight the next election, which must be called by 2007—though he insists that before then he wants to turn the corner against crime and to reform education. Even so, a party conference in September seems likely to choose a successor. As befits what has become Jamaica's natural party of government, competition is intense. What is less clear is whether the new generation will be any more successful than its elders at tackling a stagnant economy and rampant crime.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Nepal

Feudal follies

Feb 3rd 2005 | KATMANDU
From The Economist print edition

AP

An old-fashioned monarch stages an old-fashioned coup

INVOKING his ancestor, Prithvi Narayan Shah, the 18th-century founder of his dynasty and unifier of the nation, Nepal's King Gyanendra on February 1st came close to reimposing absolute monarchy. He sacked the all-party government and suspended constitutional freedoms of expression, assembly and movement, the protection from preventive detention and the rights to information and privacy. The next day he unveiled a new cabinet of cronies, chancers and nobodies, which he will chair. As dictators usually do these days, the king pronounced himself a democrat and promised to restore multi-party rule within three years.

Democracy under a constitutional monarch was introduced in 1990, and suspended by the king in 2002. But never before has he taken power so directly. Oddly, since he himself appointed the ousted government only last year, the change of government was more of a putsch. The prime minister was detained at his residence with some of his ministers. His deputy was taken into custody. Political leaders were put under house arrest. One, the head of a moderate communist party called the UML (Unified Marxist-Leninist), was yanked away from the television cameras as he was making a statement about the coup. Some intellectuals, human-rights activists and journalists went into hiding. Most now seek anonymity.

Katmandu airport was shut for a few hours and flights turned back. Armoured vehicles appeared briefly in the capital, but within a day the soldiers and riot police were lolling idly on their batons and rifles. There was little chance of organised opposition. Local telephone lines, mobile networks and internet access were all cut. Gossip, the lifeblood of the Katmandu elite, meant going out and

finding people. The king's press secretary called in newspaper editors and told them he could not help if the army decided to “disappear” them for a few hours. Censorship was absolute. One effect of this was that a three-day *bandh*, or general shutdown, called by Nepal's Maoist rebels in protest at the coup, was, unusually, ignored.

The Maoist rebellion, which has killed some 11,000 people since 1996, and now affects every part of the country, provided one of the two related pretexts for the royal takeover. The king complained about the lack of progress in reopening peace talks with the Maoists. Then he criticised the government for not making a sincere effort to hold elections by this April, to replace the parliament the king dismissed in 2002. Both pretexts are spurious. The Maoists refused to talk to the old government because it ruled at the whim of the king, who retained control of the army. Similarly, the idea that a free and fair election could be held was fanciful. The police and army have withdrawn from most of the countryside, leaving it prey to Maoist terror.

King Gyanendra assumed the throne in 2001, after a massacre in the royal palace, in which many of his family, including his brother, King Birendra, died. Gyanendra has never been a popular king. His family is accused of corruption and his son, Paras, the present crown prince, is feared and loathed. Yet Kanak Dixit of *Himal*, a Nepali journal, says he would be forgiven if he could restore peace. But that would mean either successful talks with the Maoists or winning the war. Neither seems likely.

Although the Maoists had said they wanted to talk to the king, they were not advocating a coup. Their call for a strike was accompanied by a diatribe against “feudal autocracy” and a call for a united front with the constitutional political parties. On the military front, most observers do think the army could try much harder to defeat the Maoists. But few think it capable of a decisive victory.

It will become even less capable if foreign governments cut off assistance. King Gyanendra can hardly have been expecting an international round of applause. But he must have been taken aback by the severity of the reprimands he received from governments such as Britain's and, especially, India's. Reluctance to honour the king with a prime ministerial handshake was one reason India decided to stay away from a forthcoming regional summit, leading to its postponement. There is real alarm in Delhi at the prospect of continuing anarchy in Nepal, with its effects spilling across its border with India, which has a big Maoist problem of its own.

Nepal's political parties, such as the UML and the Nepali Congress, have an exasperating record of incompetence, corruption and infighting. For this reason some foreign governments have been sympathetic to the king's authoritarian instincts. But the parties are not going to vanish, and must remain the core of the multi-party system the king says he wants.

It is the monarchy that may be in greater danger. “Forget Katmandu: An elegy for democracy”, a new book on Nepal by Manjushree Thapa, a novelist, recounts a story about King Prithvi Narayan Shah. He once met a god disguised as an ascetic who, to test his loyalty, offered him some curd he had vomited. Had the king eaten it, his dynasty would have lasted forever. Instead he tossed it aside, and some fell on his feet. So the dynasty would only last ten generations, one for each toe. King Birendra was the tenth Shah king.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA
PRINTABLE PAGE VIEW SPONSORED BY

China

The burial of Comrade Ziyang

Feb 3rd 2005 | BEIJING
From The Economist print edition

A compromise over a funeral

THE low-key funeral held on January 29th for China's former Communist Party chief, Zhao Ziyang, who was deposed in 1989 for allegedly supporting pro-democracy protesters, reflected the mood of a party leadership that still feels deeply insecure. But it also showed how adept the party has become at handling its anxieties.

The leadership feared the event might unleash an outpouring of public discontent, just as the death of Mr Zhao's liberal predecessor, Hu Yaobang, 16 years ago triggered the Tiananmen Square protests. The funeral of Zhou Enlai, a prime minister also considered something of a moderate, triggered demonstrations in 1976.

State television and radio made no mention of Mr Zhao's death, at the age of 85, on January 17th. Postings about Mr Zhao were quickly removed from internet bulletin boards. Foreign news publications, including *The Economist*, were barred from sale. Dissident activists were placed under house arrest. On the morning of the funeral, hundreds of uniformed and plain-clothes police were deployed on approach roads to the Babaoshan Revolutionary Cemetery in western Beijing where his body, draped in a red party flag, was laid in a hall prior to cremation.

Remarkably, given the tools now available to many Chinese to get uncensored news, efforts to keep the public in the dark about the funeral appeared largely successful. Only a handful of citizens gathered outside the cemetery, considerably outnumbered by foreign journalists and police, to watch the arrival of the more than 2,000 mourners who were officially permitted to enter Babaoshan.

Just as remarkably, given that Mr Zhao had been kept under house arrest ever since the Tiananmen protests, the leadership avoided the temptation to treat him the same way in death. The party allowed the family to invite anyone to Babaoshan who had turned up at the family home in the previous few days to offer their condolences. This included many people previously unknown to the family who had wanted to pay homage to Mr Zhao for his opposition to the use of military force to crush the unrest in 1989. Officials vetted the list (foreigners, journalists and outspoken dissidents were among those barred), but it was, in effect, the biggest officially approved gathering of political liberals since Tiananmen days.

AP

What is more, China's official news agency, Xinhua, reported later in the day that top officials were among those who had turned out to bow before the body and shake hands with the family. These included Jia Qinglin, the party's fourth-ranking member. It said that Vice-President Zeng Qinghong had been to visit Mr Zhao in hospital shortly before his death. Xinhua's dispatch said Mr Zhao had committed “serious mistakes” during

the 1989 unrest, but acknowledged that he had made a “contribution to the cause of the party and the people”.

Even the few non-invitees who gathered outside Babaoshan, some of them in tears and loudly denouncing China's disrespect for human rights, were treated with unusual forbearance by a police force normally inclined to lock such people up. None of this suggested any shift in the leadership's official position on Tiananmen or on Mr Zhao. But it was a grudging nod in the direction of lingering Zhaoists that deftly avoided the reopening of the party's bitter wounds. Now the question is what to do with the ashes.

You may weep, but not too much

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA
PRINTABLE PAGE VIEW SPONSORED BY

China and Taiwan

A lunar thaw

Feb 3rd 2005 | BEIJING
From The Economist print edition

Cross-strait relations are improving again

Get article background

ALL of a sudden, after months of worry about escalating tensions between China and Taiwan, the two sides are being a bit nicer to each other. On January 28th, the Chinese leadership expressed willingness to talk to Taiwan's president, Chen Shui-bian. The next day, passenger aircraft flew across the Taiwan Strait without stopping in Hong Kong or Macau, for the first time since the Communist takeover of China more than 55 years ago—hijacked planes excepted. On February 1st, Taiwan received its most senior Chinese visitors in ten years.

Could a thaw at last be under way? Both sides are avoiding saying so. Before the flights took off, carrying Taiwanese businessmen and their families home for next week's lunar new-year holiday, a Chinese spokesman said relations remained “grim”. Taiwan responded moodily to the offer of talks, saying China was still insisting that Taiwan accept the idea of “one China”. China said the officials visiting Taiwan were only there for the funeral of a Taiwanese negotiator.

But there does appear to be a shift. Taiwan's Mr Chen, who campaigned hard in elections last December for more assertive moves to express Taiwan's independence, has now appointed a moderate, Frank Hsieh, as his new prime minister. Earlier this year, China was on the offensive, calling for an anti-secession law to be passed when its parliament meets in March. Many think the law will threaten Taiwan with military reprisals should it move towards formal independence. But in mid-January China agreed to the charter flights.

Similar flights were organised in 2003, though not last year. Two years ago, at Taiwan's insistence, they had to touch down en route in Hong Kong or Macau. This time, the aircraft were allowed to fly non-stop, albeit not directly: they still had to make a lengthy detour through Hong Kong airspace on their way to and from Beijing and Shanghai.

The charter flights will cease on February 20th. Soon thereafter, tensions are likely to rise as China's legislature debates the proposed law. But amid all the heated rhetoric, a grudging accommodation is still possible, even if a lasting settlement remains a long way off.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Japan

Metimorphosis

Feb 3rd 2005 | TOKYO
From The Economist print edition

Economic change and political reform have weakened a dominant ministry

Get article background

SOME admired its influence; others decried its interference. But there was a time when nobody doing business in Japan, or with Japan, could ignore the clout of its Ministry of International Trade and Industry (MITI). Over the past 15 years, however, changes in Japan's economy and political system have been transforming the ministry's role. Since 2001, when broad economic duties were added to the trade and industry bits, it has been known as METI rather than MITI. Yet that nominal expansion of its role has belied a steep depreciation of its currency, relative to the only benchmark that Japanese civil servants care about: the power to tell others what to do.

Some of that slide reflects temporary factors. Junichiro Koizumi, the prime minister, has longstanding ties to the rival finance ministry, for example; and METI's mishandling of Daiei, a failed retailer that was taken over by a state-backed agency in October, has given it a bloody nose in the press. But METI's declining image also reflects deeper changes.

Even before Japan's bubble popped in 1990, the ministry had been losing sway. Its power was greatest during the first few post-war decades, when rapid growth and financial controls created more demand for scarce resources than the economy could supply. That allowed MITI to ration resources, and thus bend private companies to its will. The ministry had to adapt as Japan's outdated financial controls were removed, and as successful exporters such as Toyota and Sony built global businesses that were harder for MITI to control. The post-bubble collapse, however, was even harder on the ministry. The most important economic themes in the early 1990s were property prices, bank loans and spending on public works, all of them areas in which MITI was forced to be a mere bystander.

So in the mid-1990s it tried to reinvent itself, with help from a powerful politician: Ryutaro Hashimoto, MITI's minister before he took over as prime minister in 1996. Mr Hashimoto set out to streamline policymaking, giving MITI a new co-ordination role that would let it demand closely-guarded information from other ministries. Although Mr Hashimoto resigned in 1998, MITI continued to reshape itself as Japan's deregulation ministry, in a bid to tell other ministries how their policies should change. Its officials boosted their career prospects in the process. Firms that were once under the sway of other ministries had to consider hiring retirees from MITI as well, if they wanted to gauge future policy changes and cash in. The ministry's transformation seemed complete in 2001, when the overarching “economy” label was added to its name.

With hindsight, however, that now looks like its high-water mark. As Mr Hashimoto's political reforms evolved, METI ironically ended up losing influence. Japan's economic policy is now co-ordinated more effectively, just as Mr Hashimoto once hoped. But this is now done in the Cabinet Office—led in Mr Koizumi's case by Heizo Takenaka, a former academic—using officials who have been seconded from all over the bureaucracy. A former senior official from METI argues that

Japan's freedom-of-information law, passed in 1999, has also made policy formation more entrepreneurial. Now anybody with the right skills can get information from the relevant ministries and draft a reform proposal, eroding the information advantage that the ministry gained under Mr Hashimoto.

METI is not the lead ministry in any of the big policy debates of the day. Mr Koizumi is keen to privatise the post office. Other politicians are worried about pensions and health-care finances. Taxes and local-government finances are also near the top of the agenda, now that the finance ministry has claimed victory over stagnation and is pressing ahead with its long-held goal of shrinking deficits. METI still has some talented officials. But if they want to make a difference, they must now compete in a freer market for ideas.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Australia

Guantánamo comes to Sydney

Feb 3rd 2005 | SYDNEY
From The Economist print edition

Plus royaliste que le roi

Get article background

WHEN Mamdouh Habib stepped off a charter flight in Sydney on January 28th, after being held for three years without charge in the American military prison at Guantánamo Bay, his freedom was not as complete as it seemed. Australia's coalition government had all but washed its hands of Mr Habib and David Hicks, another Australian still imprisoned at Guantánamo Bay, suggesting both men had links to the al-Qaeda terrorist group. The government was taken by surprise on January 11th when the United States advised it would be laying no charges against Mr Habib.

As Mr Habib was reunited with his family in Sydney, the politicians tried to argue that little had really changed. Alexander Downer, the foreign minister, said the government had told America it would ensure Mr Habib did not become “a threat to the Australian people”. Philip Ruddock, the attorney-general, said Mr Habib would remain under surveillance and would be restricted in his travel outside Australia; he even suggested the government might try to stop him being paid for his story by the media.

Mr Habib, 48, a former cleaner, was arrested in Pakistan in October 2001, where he was reportedly interviewed by Australian intelligence authorities and police. His wife maintained he was in Pakistan looking for an Islamic school for their children. Pakistan sent him to Egypt for six months—at America's request, it said—from where he was transferred to Guantánamo Bay in May 2002. Last October, American officials said Mr Habib had confessed to giving martial-arts training to hijackers involved in the September 11th 2001 attacks, and that he knew of the attacks before they happened. Mr Habib's lawyers said the confessions were made under torture.

A ruling this week by a federal court in America that the Guantánamo Bay military review tribunals are unconstitutional brought more pressure on Australia over the second detainee. David Hicks, 29, from Adelaide, was held in Guantánamo Bay for two-and-a-half years before being charged last June with conspiracy, attempted murder and aiding the enemy; he has yet to be tried by a military commission. Could the government, its critics ask, have done more for him and Mr Habib?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

After the tsunami

The rebuilding starts

Feb 3rd 2005 | BANGKOK
From The Economist print edition

Assistance has been generous: but it is not always being well spent

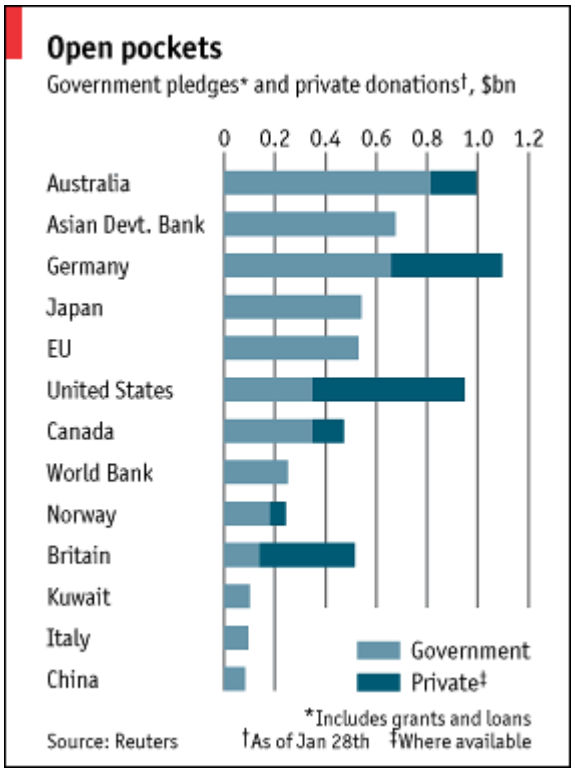
“IT IS not enough to do good; one must do it the right way.” The adage, although coined by a Victorian politician, would serve well as a motto for the relief effort following December's tsunami in the Indian Ocean. Five weeks after the waves killed some 300,000 people, and left millions more without food, homes or livelihoods, the global outpouring of money and sympathy is only just beginning to ebb. Governments, firms and individuals have given more than many aid agencies can spend, perhaps $6 billion in all. But the results of this generosity have not always lived up to expectations—and there are more pitfalls ahead.

Much has been done the right way. As Jan Egeland, the United Nations' main official dealing with the disaster, pointed out, the immediate humanitarian response proved “remarkably, perhaps singularly, effective, swift and muscular”. Despite fears that governments would not make good on their pledges of assistance, the UN has already received roughly half of the $1 billion it was promised for the first phase of the relief effort. Other aid agencies, such as Oxfam and Care, say they have enough money in the bank to pay for several years' work in the affected areas.

Nine survivors who had wandered lost in the jungle for over a month were discovered on February 2nd in India's Nicobar islands. But the basic needs of the vast majority—for food, water, shelter and rudimentary health care—are already catered for. Some schools have re-opened in Aceh, the worst-hit region of Indonesia. They have been operating for several weeks in most of Sri Lanka, India and Thailand. Boats and trucks are starting to find their way to villages that could only be supplied by helicopter at first. In Sri Lanka, the government is already starting to repair rail tracks washed away by the deluge.

All this means that the much-feared “second wave” of deaths from disease and starvation has never materialised. The emphasis of relief work is shifting from emergency response to reconstruction. America and Singapore, for example, are withdrawing the troops that rushed to Aceh immediately after the disaster (although Japan, in its biggest overseas troop deployment since the second world war, recently sent a contingent of around 950 soldiers to the scene).

But there are still gaps. An assessment mission led by the UN's World Health Organisation along Aceh's ravaged west coast found a glut of pain-killers and antibiotics, and a shortage of soap and bandages. Hand-outs of food contained too little protein, the team also said, which could lead to malnutrition. Little effort has been made to funnel aid to the most vulnerable: orphans, widows, the elderly. Officials in the Maldives complain that the world is largely ignoring their plight, perhaps because the country's relatively low death toll gives the mistaken impression that it escaped without much damage.



So much to do

In other places, a surfeit of aid agencies is making co-ordination hard. No fewer than 180 different outfits are operating in Sri Lanka. Well-intentioned but ignorant donors are sending woolly jumpers to tropical beaches, and mini-skirts to conservative Muslim areas. Others are mixing missionary work with charity, raising fears of a backlash against aid workers. Both Islamic fundamentalists and Scientologists have come to the aid of bewildered Acehnese, for example.

Politics is intruding on the aid effort. The countries around the Indian Ocean are fighting tooth-and-nail for the privilege of hosting a regional early-warning centre for tsunamis. When India, Indonesia and Australia ganged up to reject Thailand, it announced it would set up its own system anyway. China succeeded in getting Taiwan excluded from a UN conference on the catastrophe. And although the government and rebels are co-operating over the delivery of aid in both Indonesia and Sri Lanka, there is little prospect of a lasting settlement in either country.

Meanwhile, the repercussions of the tragedy continue to spread. The number of people unable to feed themselves continues to rise, as food stocks and savings run out and as villages spared from the waves are engulfed by the economic turmoil that has followed. As Geoffrey Dennis, of Care UK, points out, many other regions of Sri Lanka exported labour to the tourist resorts of the south, and so are beginning to feel the pinch of the current slump.

Reuters

There is also a risk that the authorities may over-react, and introduce ill-considered new policies. Ashvin Dayal, head of Oxfam in East Asia, warns that governments and other aid agencies must be careful to consult survivors about their wishes, and not simply impose their pet reconstruction plans. Fishermen in Sri Lanka are already up in arms about a scheme to relocate their villages farther from the shore. Researchers at the Stockholm Environmental Institute, a think-tank, are worried that donors are placing too much emphasis on expensive technical schemes, such as the disputed early-warning system, and not enough on all-round disaster preparedness at the village level.

Furthermore, aid agencies seem torn between the fear that the world will soon forget about the catastrophe and the concern that the tsunami is eclipsing other equally worthy causes. This week Kofi Annan, the UN secretary-general, appointed Bill Clinton as his special representative on the relief effort, with a brief to help sustain international interest. Only a few days earlier, the head of the UN's Children's Fund had called an end to fresh fund-raising for tsunami victims, while encouraging donations for children in need in 33 other countries instead.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Iraq's elections

Can the voters build on success?

Feb 3rd 2005 | BAGHDAD
From The Economist print edition

Getty Images

In four articles on Iraq's elections, we analyse the elections' achievement—and see why a new government will still struggle to impose itself, at home and abroad

Get article background

"A GREAT day," said the interim (and perhaps outgoing) prime minister, Iyad Allawi. "Absolutely delighted," was the verdict of a usually dour American diplomat in Baghdad. Many Iraqi voters evidently shared such feelings, dancing in the streets, tossing sweets into polling stations, and waving two fingers, one dyed with supposedly indelible ink to prevent multiple voting, in a victory salute. Many said that the vote was a defeat for terrorism and that their sons and fathers murdered by Saddam Hussein had now been avenged. "I'm a suicide voter!" proudly declared one of the first citizens to cast a ballot in a Sunni district of Baghdad.

It was not all joy. At least 44 people, including 26 Iraqi civilians, eight Iraqi troops, ten British servicemen and one American soldier, are known to have been killed on election day. All told, across the country, insurgents launched a record 260 attacks, four times the current daily average, in an attempt to wreck the vote. There were around 100 attacks at or near polling stations, of which there were more than 5,300. Faced with a total ban on vehicle traffic throughout the country, the insurgents sent at least eight bombers on foot, wearing suicide vests, into voting stations. But no polling station was burned down or blown up.

As expected, the Sunni Arabs' turnout was small. Early estimates put it at 20-30%. It was almost non-existent in well-known trouble spots such as Ramadi, Fallujah and Samarra. But in mixed areas, in Sunni districts of Baghdad, in Mosul (a mixed city where the insurgency has been

especially fierce of late), in tribal areas and in various places across the Sunni triangle, the vote was much higher than expected—though hundreds of thousands of voters in Sunni Arab areas either voluntarily boycotted the poll or were frightened away.

Certainly there were irregularities. Some polling-station officials made helpful suggestions as to which list voters should tick. In some areas, party toughs kicked rivals' poll-watchers out of the stations and tampered with the ballot boxes. Some Kurds discovered that the ink used to prevent double-voting was actually quite delible if you first dipped your finger in moisturising cream.

American army officers say that the insurgents were less effective than had been feared, for two reasons. First, they have recently lost many of their best men, including Baathist officers trained in guerrilla warfare. Many insurgents thrown into the fray to disrupt the election were apparently raw recruits. Second, the Iraqi security forces performed better than usual, perhaps because they too were inspired by the feeling that it was an historic opportunity for their compatriots to have a genuine choice at the ballot box for the first time in living memory. Just before election day, it was notable that many watching youths cheered when the tanks of the new army's first mechanised brigade, decked in national flags, rolled through central Baghdad, looking like a real fighting unit.

A sense of “taking back the streets” was visible on election day, especially in Baghdad. Even the Mahdi Army, the militia of the fiery Shia, Muqtada al-Sadr, who had discouraged his followers from voting without exactly telling them not to, helped keep order in Baghdad's slums, making it easier for citizens to go to the polls.

This mood of hope, almost euphoria, may explain why none of the big parties has complained about electoral irregularities. The worst organisational defect was a shortage of ballot papers in certain areas, especially in the Sunni Arab north; in Mosul, the papers twice ran out, according to Ghazi al-Yawar, a Sunni Arab with a tribal following who is the interim president and headed his own electoral list. But even the smaller parties, who lack toughs of their own and for whom a few thousand votes could make the difference, under the system of pure proportional representation, between getting a seat in parliament or not, have so far been fairly reluctant to shout foul.

Though full results may not be known for ten days after the poll, it is still considered most

probable that the most votes have been cast for the United Iraqi Alliance, better known as “the Shia house”, “the clerics' list”, or simply “list 169” after its number on the huge ballot paper. Though Grand Ayatollah Ali al-Sistani, Iraq's most influential clergyman, did not formally endorse the list, his bearded visage was emblazoned on its posters.

Its two key components are two Islamist-inclined parties, the Supreme Council for Islamic Revolution in Iraq (SCIRI), led by a cleric, Abdul Aziz al-Hakim, and the Dawa (“Call”) party, led by a doctor, Ibrahim al-Jaafari. In the run-up to the poll, both parties sought to soften their Islamist tinge (and especially SCIRI's close ties with Iran) in a bid to reassure Iraq's many secular-minded Shias that they do not intend to turn Iraq into an Iranian-style theocracy. Some of its posters even featured attractive unveiled women.

The rival Iraqi List, headed by the secular-minded Mr Allawi, may also have done well. Many Sunni Arabs seem to endorse his wish to rebuild a strong army and see him as a bulwark against an Iranian takeover, while members of both main Muslim sects like his sturdy leadership style—“like Saddam but with justice”, as a Sunni voter put it.

Provided that the clergy-backed United Iraqi Alliance does not win an outright majority, which some of its adherents are predicting, some frenzied horse-trading is likely to take place in the next few weeks, as parties jockey for a place in a ruling coalition. Mr Allawi's list and the Kurdish Alliance, which is sure to have swept up most Kurdish seats (see article), may well hold the balance. But even Communists and monarchists may play a pivotal part.

The next step is for the 275-seat assembly to choose, by a two-thirds majority, a three-person presidential council (a president and two deputies) which in turn must unanimously choose a prime minister within a month of the election. The assembly must then endorse a prime minister and his chosen government.

All the main parties say they will ensure that Sunni Arabs are well represented, both in government and in the committees due to draft a constitution. This should be ready in mid-August, endorsed in a referendum in mid-October, and pave the way to another general election, under new rules, in December. But only if Sunnis are seen to have a proper say is there a chance that the new government, especially in the four worst affected of Iraq's 18 provinces, will start to contain the still raging insurgency.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Iraq's Kurds

They're on a roll, for now

Feb 3rd 2005 | SULAYMANIYAH
From The Economist print edition

Why the Kurds think they're winners—and why they should be diplomatic

Get article background

ON THE eve of the election in the Kurds' two main cities, Arbil and Sulaymaniyah, youths linked arms and danced, Kurdish-style, in the streets. Drivers honked horns as passengers hung out of windows, cheering and waving Kurdish banners. Local television stations beamed stirring historical footage of *peshmerga* fighters in the mountains, with a voice-over telling Kurds it was time to channel their revolutionary spirit into the ballot box.

In the Kurds' self-rule area, people voted for three layers of representation—three provincial councils, a Kurdish regional parliament with 111 seats, and a national assembly in Baghdad. The entire exercise, in Kurdish eyes, was a triumph, albeit just a big step on the way to guaranteeing extreme autonomy in a soon-to-be-drafted federal constitution.

Another reason for the happiness was that the Iraqi Kurds' two main parties, Massoud Barzani's Kurdistan Democratic Party (KDP) and Jalal Talabani's Patriotic Union of Kurdistan (PUK), had harmoniously forged a pre-electoral pact (a stitch-up, said a few critics). Together they are sure to dominate the Kurdish regional assembly in Arbil. Each party took 41 seats, most of the rest going to mild Islamists, Turkomen, Christians and Yazidis (followers of a sect that is said to descend from Roman-era worshippers of the god Mithras), nearly all with the blessing of the two big Kurdish parties. The often bitter and occasionally violent rivalry between the pair was tested only in the provincial elections, where each one duly prevailed in its strongholds—the KDP in Arbil and Dohuk in the north, the PUK around Sulaymaniyah and to the east and south.

The Kurds were especially chuffed by early election results for a provincial council (outside their present self-rule area) in the disputed province of Kirkuk, which they look set to dominate with a reported 60% of the vote. The results there and in Ninewa province, which includes the equally disputed (and recently much bloodier) city of Mosul, appear to reflect a shift in the balance of power of the Kurds in the north—which alarms many Iraqi Arabs—as well as Turkey's and Iraq's Arab neighbours.

In a likely share-out of top jobs, Mr Barzani said he would back his old rival, Mr Talabani, for a plum job in Iraq's national capital—either as prime minister or president—while he would expect the top job back home. Both Kurdish leaders sound happy to join a coalition government in Baghdad, with either the main Islamist-inclined Shia alliance or with a more secular-inclined list headed by the interim prime minister, Iyad Allawi. By forging a united front, the Kurds will bolster their strength in the national assembly in Baghdad (where they may even hold the balance) and secure a key spot in Iraq's post-election constitutional debate. As before, they are sure to demand de facto independence, autonomy over finance, control over Kirkuk province, a fixed percentage of Iraqi revenues, and even control over Kurdistan's minerals.

They must, however, be careful not to overplay their hand. Turkey, for one thing, has again implied that the Kurdish acquisition of Kirkuk could spark civil war—and even a Turkish intervention.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Iraq's south

Worrying trends

Feb 3rd 2005 | BASRA AND ZUBAYR
From The Economist print edition

The Islamist ascendancy down south is not entirely reassuring

AFP

The men of Zubayr come to make their choice

Get article background

FOR the first hour of polling, there were almost no voters in Zubayr, a troubled town of 400,000 souls in southern Iraq, some 15 miles (24km) south-west of Basra. But nor were there bombs. And, suddenly, voters came swarming. Along rutted, rubbish-strewn streets traipsed stern tribesmen and black-cloaked women, silently congregating at polling stations festooned with brightly-coloured ribbons and balloons and banners praising God.

So went Iraq's elections across the south, a poor, mostly Shia Arab region, occupied by 9,000 British troops. Basra, the south's once cosmopolitan capital, saw outbursts of joy. Tearful people danced in the streets and flourished the inky forefingers that marked those who had voted. The city also saw violence: a few mortar shells, launched by unknown insurgents, flew harmlessly across it. But these were the dampest of squibs compared with what had been expected. In Zubayr, where Sunnis make up about a third of the people, sectarian murder is common, but the only fighting was between policemen, after one police station's occupants mistook another's celebratory gunfire for an insurgent attack.

In Basra, according to early estimates, turnout was over 70%; in Safwan, on the border with Kuwait, it was 80%; in Um Qasar, Iraq's biggest port-town, 75%. Given that Shia clerics had ordered their followers to vote, this was predictable. Yet even in Zubayr, where Sunni preachers had raged against the election, over 60% of registered voters turned out, and it was plain that many were Sunni.

One beefy Sunni farmer, Raad Triag, had brought his wife, mother and two sisters to vote for the list headed by Iyad Allawi, Iraq's interim prime minister, a secular Shia he considered admirably tough. While most other candidates for the national assembly were too frightened to reveal themselves, Mr Allawi made his second official visit to Basra on January 22nd—after raising civil-service salaries by $100 a month.

The main contest in the south was between those Shias who want a more Islamist-leaning state (most of them supporters of the United Iraqi Alliance) and those, like Mr Allawi, who favour a more secular one. Rumours in Basra were rife that the Islamists had infiltrated the local electoral commission. Many security as well as administrative posts in Basra's provincial and town councils are already held by Islamists, and many secular-minded Iraqis felt that Islamists had too big a role guarding polling stations and transporting ballot boxes. A striking number of observers in Zubayr's polling stations wore beards.

To the secular-minded, the record of Basra's mainly Islamist local rulers is not reassuring, despite recent efforts to play down their Islamist intentions. In recent months, Islamic strictures have been tightened across the south. Even in Basra, alcohol and music shops have been closed and women arrested for prostitution, often on slender evidence. Yet the Islamists have done poorly at cleaning up and improving public services; Basra is one of the most decrepit and smelliest of Iraq's cities. Many of the ruling Islamists are patchily educated, having spent their youth bearing arms in Iran.

Despite the relative calm in which the election passed, the south remains perilously crime-ridden. By night, Basra echoes with gunshots. The board of the city's chamber of commerce resembles a support group for victims of kidnapping; its members say they have collectively stumped up several hundred thousand dollars in ransoms in recent months. Each, on average, spends $3,000 a month on bodyguards, and donates much of his profit to local tribesmen in the hope of persuading them not to sabotage his business.

Disgruntled Sunnis tend to get blamed for such violence. But, perhaps more worryingly, there is bad feeling in the south between Shias too. The most petulant Shia leader, Muqtada al-Sadr, whose fighters set southern Iraq ablaze in August, is not on an electoral list, though a score or so of his followers are, and most of his people have refused to endorse the election. On the peeling walls of a polling station in Basra, bright red graffiti read “Down with America! Death to Allawi! Pray with Muqtada!” A new government will have to ensure not just that it reaches out to Iraq's Sunni Arabs but also that it deals, one way or another, with Mr Sadr's numerous and fiery disciples.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The Arab neighbours

The fear of contagion

Feb 3rd 2005 | CAIRO
From The Economist print edition

Some pretended it hadn't happened, others dreamt of it happening at home

Get article background

THERE are many versions of Iraq's recent history, but the one most widely shared in neighbouring countries has been black and white, like an old newsreel: a poor Muslim country is blitzkrieged by a ruthless Christian army which installs a quisling government, so inspiring a noble, patriotic resistance movement. But if Iraq's bloody complexity has often made it hard to sustain this comforting narrative, the unmistakable imagery of a truly popular election, at least in most parts of the country, has now rendered it untenable.

Not that some don't keep trying. In undemocratic Syria and Egypt, the dominant, government-owned press played down the poll. The Cairo daily, *al-Ahram*, put it on its front page, but squarely below the fold. Syrian state television focused single-mindedly on election-day violence rather than the voting itself. Several Arab newspapers ran cartoons showing Iraqis voting at the point of an American gun. Even al-Jazeera, the pretty independent satellite channel beamed out of Qatar, peppered its far fairer reporting with large dollops of scepticism, highlighting the low turnout in Sunni Arab areas, voting irregularities, and fears of rising Shia dominance.

But some in the region have always seen things differently. Minority groups such as secular liberals, Kurds, Algeria's Berbers, and Shias, tend to sympathise with the historic victims of Arab nationalism, such as the non-Sunni Arab majority of Iraqis who turned out to vote. Such feelings do not have to translate into approval of America's invasion, but they contribute to a counter-narrative that sees hope, rather than despair, rising from its ashes.

This different version could be seen, for instance, in the breathlessly enthusiastic coverage of the election by al-Jazeera's rival, al-Arabiya. In the weeks before, the Dubai-based, Saudi-owned station had run a series of adulatory interviews with Iyad Allawi, Iraq's interim prime minister, as well as saturation advertising to get out the vote. For the big day it carried feeds from eight different places across Iraq.

In fact, the run-up to the election witnessed a more general movement of regional opinion towards the friendlier end of the al-Jazeera/al-Arabiya spectrum. Hizbollah, Lebanon's Iran-backed Shia militia, dropped its sharply critical line on Iraqi affairs in favour of celebrating Shia gains. In Iran, similarly, the official view was that the elections were a good thing, though the head of the Islamic Republic's Revolutionary Guards said this was because the vote had struck a blow against America.

In recent months, the more thoughtful of Arab press commentators have increasingly embraced the idea of elections, if only because they were seen as likely to lead, in the longer run, to ending the American occupation. At the same time, the Iraqi insurgency's apparent lack of a coherent

programme other than violence has whittled away much outside support. The fact that the most extreme of Iraq's Sunni Islamist groups denounced not just these elections, but democracy in general, did not win more converts.

One theme that has continued to resonate, in some quarters, is the supposed danger of empowering Iraq's Kurds and Shias. Turkey, Syria and Iran, worried about their own restive Kurds, shaded official praise for the polls with traditional hints that Iraq's Kurds should keep their heads down.

Fears of a “Shia menace” are vaguer but more widely shared. Since Iran's 1979 Islamic revolution, rich Gulf monarchies have worried about the export of Shia fervour to their own countries, where they make up some 12% of the 20m indigenous Arabs. Saudi's Wahhabist version of Sunni Islam regards the Shia creed as an aberration, and it does not help that the kingdom's Shias happen to be concentrated in the oil-rich Eastern Province. In tiny Bahrain, Shias are 60% of the population—and have long wanted a fairer share of power.

Shia leaders in the Gulf are keenly aware of the suspicion with which many regard them, and argue convincingly that they do not want to see an Iranian-style Islamist state emerge in Iraq or elsewhere. Yet the rise of Shia power in Iraq may start to encourage demands for greater enfranchisement. Bahrain's four main opposition groups have grown louder in demanding constitutional reforms to curb the ruling Sunni family's powers. In Saudi Arabia, the Shias have mobilised in advance of municipal elections to be held over the coming months. Voter registration is running far higher in the Eastern Province than elsewhere in the kingdom.

This underlines a deeper fear in Arab ruling circles, which is that people power may prove infectious. Even under occupation, Iraq's expression of popular will provided a stark contrast to the lot of other Arabs. Saudi Arabia's elections, for instance, are for only half the seats on toothless town councils, with half the populace—women—excluded. In the week of Iraq's election in the most populous Arab country, Egypt, police arrested a leading liberal opposition MP, ten Muslim Brothers and a group of leftists who had called for real, contested presidential elections, rather than another rubber-stamp referendum such as is scheduled for later this year.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Land rights in Israel

Keeping control of Jerusalem

Feb 3rd 2005 | JERUSALEM
From The Economist print edition

Israel's attempts at land control meet an obstacle

Get article background

WHAT began as bad news has quickly turned into good. A fortnight ago Israel's liberal *Haaretz* newspaper revealed that, last summer, the government had quietly decided to start using an old law to confiscate hundreds of hectares of Palestinian-owned land in East Jerusalem. The scandal, and perhaps some pressure from America's new secretary of state, Condoleezza Rice, provoked a climbdown. Israel's attorney-general, Menachem Mazuz, said he had not been told; the prime minister's office said he had; and this week he recommended scrapping the decision.

The timing helped. With a new Palestinian president in office and a fragile, impromptu ceasefire just barely holding (there has been violence, but both sides have held back from major reprisals), Israel cannot afford to look recalcitrant.

But the fight for Jerusalem's land is far from over. The 1950 Absentee Property Law, which will remain in force, allows the state to confiscate land within Israel if its owners have spent any time at all away in the Arab countries where most Palestinian refugees wound up. Though Israel annexed East Jerusalem in 1967, thus making it “within” Israel (though not in most international eyes), it decided not to apply the law there. With rare exceptions, Palestinians who owned property within the city boundary but lived just outside it in the West Bank kept their land.

But since last summer the law, together with the barrier that Israel is building, ostensibly only to keep out terrorists, has changed that. Some owners have found their houses outside the barrier and their olive groves inside it. Even if they technically get their land back after Mr Mazuz's recommendation, the wall will not move.

Nor does it always follow Jerusalem's boundary. It will, for example, exclude al-Walaja, a village to the south-west, though half the village is inside the city limits. All the same, residents in the “Israeli” half are frequently harassed for not having Israeli residence permits, as other Jerusalem Palestinians do; they never got them because the fact that they lived “in” Jerusalem was somehow overlooked until the 1980s.

Moreover, there are other ways to get people off the land than declaring them absentees or illegal residents. In al-Walaja, 30 of the 80-odd houses face demolition orders for illegal construction, says Meir Margalit of the Israeli Committee Against House Demolitions, which is lobbying to stop them. Building permits are notoriously hard and expensive to get, so demolition orders are easy. In Sur Bahir, a few miles to the east, another pretext—security—is behind a proposal to knock down any houses within 500 metres of where the barrier will pass, even though elsewhere around the city, such as in Abu Dis, houses have remained standing right up to the wall.

All in all, says Mr Margalit, the house demolitions fit in with a strategy of making space to join up the Israeli settlements south of Jerusalem in a continuous chain, making it harder to give up those areas in any future peace deal. Al-Walaja and Sur Bahir are right in the middle of that chain.

Legal challenges to individual bits of the barrier route have had a few successes; this week a modified route is due to go to the cabinet. Changes include allowing a village to keep its cemetery. But the barrier will still sever economic and social ties between Palestinians inside and outside its confines.

In addition, says Orna Kohn of Adalah, a legal-advice centre for Arabs, this summer the army is expected to start enforcing more stringently the ban on Israelis visiting Palestinian-controlled areas, which up to now has been ignored for non-Jewish Jerusalemites. They will need permits to visit relatives across the barrier: another way of isolating Jerusalem from the rest of the Palestinian territories.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

South Africa

Counting the cost of denial

Feb 3rd 2005 | JOHANNESBURG
From The Economist print edition

New efforts to assess the epidemic

WHAT is the death toll from AIDS in South Africa? There is no easy answer. Graveyards and memorial pages in newspapers make it plain that young people, especially women, are dying in droves. Last month Nelson Mandela, the former president, said that one of his sons had died of AIDS. Official figures from 2003 show 5.6m people infected, in a population of 45m. But death statistics are much murkier. According to a model developed by the Actuarial Society of South Africa, 1.2m South Africans had died of AIDS by the middle of last year.

A mortality report by the official statistics agency is due out this week, describing the cause of death among patients between 1997 and 2003, when the impact of AIDS grew sharply and the death rate rose. Amid suspicions of political interference, publication has already been delayed. The government is loth to admit how many people are dying while it remains slow to provide drugs to keep the infected alive. The president, Thabo Mbeki, has been notoriously reluctant to acknowledge the horrifying spread of AIDS and its causes.

Doctors are often reluctant to note deaths from AIDS, which is not a notifiable disease. Some of the bereaved are ashamed. Some want another disease recorded so that life insurance can be paid out. Diseases such as tuberculosis are often recorded on certificates, when HIV is the underlying cause of death.

Now independent researchers at South Africa's Medical Research Council (MRC) have published their own study, concluding that a huge number of AIDS deaths are covered up. By measuring the sharpness in the rise of young patients who officially die of tuberculosis or other infections while they are most likely to have been infected with HIV, the MRC says it has been able to make a good estimate of the actual AIDS toll.

Some 153,000 people actually died of AIDS in 2000, it reckons, but only about a third were officially recorded as AIDS. The rest were noted as victims of “opportunistic” diseases instead. For example, tuberculosis officially killed 49,000 people in the period, but of those deaths 28,000-plus should be put down to AIDS instead, says the report. It lists another eight diseases often similarly cited instead of AIDS.

Underplaying AIDS helps the disease kill more people than it should. If higher figures were admitted, the government might do more to tackle the scourge. Late last year, only 65,000 South African AIDS-sufferers were using anti-retroviral drugs to stay alive, of whom two-thirds were getting their pills privately. The government is proceeding slowly in its effort to get more patients on to the drugs in state clinics and hospitals. Perhaps 300,000 South Africans died of AIDS last year, says the Treatment Action Campaign, a lobby. Most of them could have been saved—or have had their lives prolonged—with the right treatment.

Mozambique

The rights to prosper

Feb 3rd 2005 | MOçAMBIQUE ISLAND
From The Economist print edition

The prospects of one island could offer a lesson for the rest of the country

VISITORS are charmed by the narrow streets and shady squares of Moçambique Island, a remote town that is part of northern Mozambique and sits, just off the coast, in the Indian Ocean. With several hundred elegant and brightly-coloured stone houses built by Portuguese colonists centuries ago, when Moçambique was their capital, it has some of Africa's most striking architecture. A whitewashed church, one of 14 old religious houses, may be the oldest still standing in the southern hemisphere. The town is a UNESCO world heritage site. A 16th-century Portuguese fort stares out over it all.

But walk on the sandy beaches to watch the sailing *dhows*, and the charm evaporates. Between heaps of broken glass and rusting railings lie mounds of rubbish and human faeces. Squatters light fires among blackened tumble-down, piles of rubble. Fig trees sprout from gaping cracks in roofs and walls.

All of Mozambique suffered during nearly two decades of civil war that ended in 1992. Refugees overwhelmed the town, tripling its population to 42,000. Even with peace they refuse to go back to villages that lack electricity, schools or piped water. After 300 years of gentle decline, it took just three decades for the old capital to rot almost beyond rescue.

State donors—Norwegian, American, Japanese—have offered to chip in. But Gulamo Mamudo, the town council's head, says private money is needed to help drive renovation. “Many people are interested in investing here. But a fundamental problem is the state housing agency.” Most buildings were nationalised on independence in 1975. Private ownership is now allowed in theory, but few have papers to prove it. Few maintain their homes: getting a loan to mend your house from the island's only bank is impossible without a title deed.

Those eager to invest—mainly rich foreigners—are mostly barred by the state housing agency. One South African, who bought and restored a house dating from 1550, first had to form a Mozambican company and make a local friend its boss. “Foreign investors are looked on as second-class,” he complains. “All these land regulations keep people away.” He knows of many outsiders who come to the island, keen to set up hotels and tourist firms. Most leave frustrated and confused by hostile property rules and demands for bribes.

The country's newly elected president, Armando Guebuza, who took office this week, is a businessman keen to lure foreign investors, even though his ruling Frelimo party is still socialist in name. A useful first step would be to simplify and relax those property rules. That might be risky politically: many Mozambicans mutter that foreigners, especially South Africans, try to buy up everything. But he could declare an experiment on Moçambique Island, letting foreigners buy title deeds so they can bring in private capital. If investment and jobs followed, it might be a model for the rest of Mozambique.

German politics

The come-back chancellor

Feb 3rd 2005 | BERLIN
From The Economist print edition

Gerhard Schröder may just have bounced back too early

AH, TO be loved again. “Let's welcome the chancellor of reforms,” were the words that met a visibly tickled Gerhard Schröder at the World Economic Forum in Davos. Things are looking up at home, too. For the first time since the 2002 election, a poll has put the ruling left-of-centre coalition ahead of the opposition. A year ago, anybody predicting such a change would have been laughed at. After a string of disastrous elections, the question was not whether Mr Schröder would go, but when. Last March he resigned as leader of the Social Democratic Party (SPD). In the summer, he faced huge protests against labour-market reforms. Pundits had him leaving this May, after another election loss in North Rhine-Westphalia, the heartland of the Social Democrats.

Now some are suggesting that Mr Schröder has a good chance of winning a third term in September 2006. But can his amazing recovery last? The question is more pointed after this week's announcement that unemployment now exceeds 5m, a post-war record—though the figure is not seasonally adjusted, and partly stems from labour-market reforms in January.

To understand the SPD's bounce-back, it helps to consider why it dropped to almost 20% in the polls last year. Mr Schröder's economic reforms, known as Agenda 2010, were unpopular, erratic and badly communicated, both to voters and to party members, who quit in droves. And the opposition, led by Angela Merkel of the Christian Democratic Union (CDU), offered an attractive alternative. Yet now Germans seem to have accepted the case for economic reform. When Mr Schröder refused to give in to protests, they admired his seriousness and resolve. In other ways, too, they seem more in tune with him, for instance when he criticises the whining to which Germans so often default. It also proved clever to hand the party leadership to Franz Müntefering. Of pure SPD bedrock, “Münte” has reconciled the party's soul with Agenda 2010, while offering it a few left-wing gestures. This has let Mr Schröder find a new role as a sort of chancellor-president, who hobnobs with the powerful abroad and enters the fray at home only when big issues are at stake.

Even as the government has got its act together, the opposition has done its best to self-destruct. For months, the CDU and its Bavarian sister party, the Christian Social Union (CSU), bickered over health-care reform. Then two key CDU leaders quit: the party's economic guru, Friedrich Merz (because he had had enough), and its secretary-general, Laurenz Meyer (because he had failed to admit to making money on the side). The Free Democrats (FDP) are not in a much better state, with a generally unimpressive leadership.

If national elections were held now the government would probably win, since the SPD's coalition partners, the Greens, who have just celebrated their 25th anniversary, have also gained ground recently. A big test will be the state election in Schleswig-Holstein on February 20th; and, even more, the election in North Rhine-Westphalia, the most populous state, on May 22nd. In both, the SPD and the Greens were on the ropes but have recovered, if not yet by enough.

Even if the ruling coalition wins both states, however, the 2006 election will not be a given for Mr Schröder. He faces three main challenges. The first may be the easiest to overcome: his government is still prone to making unforced errors. One recent example was the plan to move a national holiday from October 3rd to the first Sunday in October, to boost growth and tax revenues. After protests that the government was putting economics above national symbols, the plan was shelved.

The second challenge Mr Schröder can do little about, in the short run: the economy, and especially unemployment. Even by its own rosy forecasts, the government expects the economy to grow by only 1.6% in 2005, and unemployment to average 4.5m. This explains why Mr Schröder is so keen to gut the euro-zone's stability and growth pact: more cuts to trim the budget deficit would weaken a domestic demand that is already too feeble.

Mr Schröder's third challenge will be the most interesting. At present he shows no inclination to push ahead with the further reforms that are clearly needed. Many of his Agenda 2010 measures still have to be implemented, he argues, and society can digest only so much at a time. But after the state elections he risks coming across as somebody who wishes to sit things out. Unfortunately, Mr Schröder is unlikely to go for an Agenda 2020.

Much will depend also on whether the opposition gets back on track. Some observers predict that, if the CDU loses both state elections, Ms Merkel will have to make way, perhaps for the increasingly popular Christian Wulff, the premier of Lower Saxony. But it would be a mistake to underestimate her own will to reach the top. She has just installed a new secretary-general, Volker Kauder, a staunch conservative and good organiser, who could become the CDU's Mr Müntefering.

Like an athlete facing a race, Mr Schröder must realise the danger of peaking too early. But it no longer seems to faze him. He has let it be known that, if he has to step down after two terms, it would be no catastrophe. German chancellors usually stay for only eight years; Helmut Kohl lasted longer only because of unification. And, as *Die Zeit* recently pointed out, Mr Schröder has an appealing alternative to another election victory: Viktoria, the three-year-old orphan from Russia whom he and his wife adopted last summer.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Denmark

Full Fogh forward

Feb 3rd 2005 | COPENHAGEN
From The Economist print edition

The centre-right heads for victory in next week's election

ANDERS FOGH RASMUSSEN, who leads a centre-right coalition with support from the anti-immigrant Danish People's Party, seems sure to win Denmark's general election on February 8th. All 32 opinion polls since the election was called on January 18th have given the government a lead of between seven and ten points over the Social Democrat-led opposition. This suggests that the government may win as many as 100 of the 179 parliamentary seats, up from 94 in 2001, and that the Social Democrats face their worst result since before the first world war.

Several factors lie behind Mr Fogh Rasmussen's popularity, but the most surprising may be the welfare state. Polls suggest that most voters see him, and not the opposition leader, Mogens Lykketoft, as the best guarantor of their social system. A centre-right party might be expected to favour the greatest level of individual freedom and the least interference by government, whereas the Social Democrats were the architects of the welfare state.

Yet Danes' attitudes have changed. Most still see free education, free health care, cheap child care and high-quality services for pensioners as their birthright. But they are increasingly reluctant to pay for them with high taxes. Denmark's tax burden is second only to Sweden's among European Union countries. This has turned Mr Fogh Rasmussen's cap on tax and other fiscal adjustments, which he promised in 2001, into a runaway success. The prime minister says his tax cap, tax cuts and cuts in duties on booze and cigarettes have put a yearly DKr17,000 ($3,000) more into the average family's pockets. Meanwhile, such family-friendly initiatives as longer maternity leave and shorter hospital waiting lists have persuaded voters that Mr Fogh Rasmussen is not bent on dismantling the welfare state. Such adjustments as denying teenagers the dole are seen as necessary tweaks, not a conservative revolution.

Mr Fogh Rasmussen has made much of his ability to keep promises. In 2001, he pledged to curb immigration, cap taxes and crack down on crime. Relatively few voters care that the country's restrictions on immigration, strongly backed by the Danish People's Party, have soiled its liberal reputation abroad. Public opinion has swung against the Iraq war, and two-thirds of Danes want their 500 troops home soon, but they are unlikely to punish Mr Fogh Rasmussen for sending them.

Both the main parties kicked off their campaigns with a *smorgasbord* of promises. But to many voters, these promises are indistinguishable. Mr Fogh Rasmussen and Mr Lykketoft both say they will create jobs, boost education, improve child care, keep a tight rein on immigration and put more money in people's pockets. Such duplicated pledges make personal appeal decisive. Here too Mr Fogh Rasmussen has the edge. Mr Lykketoft is experienced and cerebral but uncharismatic. A makeover in which he shaved off his goatee beard and acquired a new haircut has not helped. Only a serious blunder by Mr Fogh Rasmussen in the last few days could swing it for the hapless Social Democrats now.

Europe's Roma

Poor and unloved

Feb 3rd 2005 | BUCHAREST
From The Economist print edition

A new attempt to improve the lot of the Roma

EIGHT central European states and a slew of international institutions launched a “Decade of Roma Inclusion” this week. That may give them just enough time to make a start on the problem, at least. Europe's 7m-9m Roma (gypsies) are its biggest and poorest ethnic minority. Their social and economic indicators veer from the bad to the catastrophic, especially along the European Union's eastern borders. Roma unemployment in Slovakia hit 87.5% in 2003. Poverty rates everywhere are horrifically high (see map).

The organisations supporting the decade, which include George Soros's Open Society Institute, the World Bank, the European Commission and the United Nations Development Programme, will help governments to carry out ten-year plans focusing on education, employment, health and housing. Some new money will also be available. In December a donors' conference pledged $42m for a Roma Education Fund. But the main aim is to get governments to give more help to Roma from existing budgets, and to make better use of the funds already available from international institutions. The EU points out that its regional fund—which disbursed €26 billion ($29 billion) in 2003—is meant not only for roads and bridges, but also for human development. Roma projects could well qualify.

Central European governments have often dealt brusquely with Roma problems in the years since communism collapsed. Times were hard for everybody, most governments felt; the Roma were not exactly popular with voters; and displaying big social problems might even set back their

hopes of EU entry. But with membership mostly achieved or assured, and incomes rising, they now have less excuse for looking the other way.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

France and America

In search of repairs

Feb 3rd 2005 | PARIS
From The Economist print edition

Both sides of an awkward relationship seek to mend fences

Get article background

"FORGIVE Russia. Ignore Germany. Punish France." This dictum was apparently coined by Condoleezza Rice at the height of the transatlantic fall-out over Iraq. Next week, as America's secretary of state, she visits Paris, to prepare the ground for President George Bush's European tour later this month. With Paris off his itinerary, yet German and Russian summits on, is this the promised snub to France?

Officially, the French and Americans insist that nothing symbolic is intended. Mr Bush dropped in on President Jacques Chirac last June. When Mr Chirac sent re-election congratulations to Mr Bush, in a letter that began with a handwritten "Cher George", the American president invited him to Washington. The French had hoped to fix this visit before Mr Bush's European trip. The difficulty, say the Americans, was finding a date. Yet they plainly had no interest in rolling out the carpet for Mr Chirac ahead of Mr Bush's own "fence-mending" visit. Instead the two presidents will dine together on February 21st on neutral territory: Brussels.

If there is a slight, the French are making light of it. Even before the Iraqi election, they recognised that they had to bury past differences and deal with Mr Bush for four more years. Michel Barnier, the foreign minister, urged "a new start" in Franco-American relations. Mr Chirac said he hoped that Mr Bush's second mandate would create an opportunity "to illustrate the vitality of the transatlantic tie". On such matters as Afghanistan, Kosovo, Lebanon, Haiti and Côte d'Ivoire, the French and Americans work well together.

Yet the deep distrust over Iraq and general mutual suspicion remain. Only 11% of the French would have voted for Mr Bush, according to a Louis Harris poll; 82% said he had made the world a more dangerous place. "His re-election would be a catastrophe for the world," declared the cover of *Le Nouvel Observateur* last September. Even now, there is little public debate in France about Iraq. In private, when asked whether the French should do more to help the Americans in Iraq, one minister snapped: "We wouldn't do it to help the Americans, but to help the Iraqis."

Which is why the election in Iraq was in some ways so awkward for France. In a telephone conversation with Mr Bush, Mr Chirac called it an "important step" and confirmed "the readiness of France to co-operate with Iraq". For the first time, there is talk of a rapprochement. Yet France is caught between grudging acceptance of the poll and lingering indignation over how it came about. "It would be difficult, if not indecent," wrote *Le Monde* in a vexed editorial, "to reproach him for having offered the Iraqis free elections."

The bottom line is that the French have not changed their position on Iraq. They will not send troops, not today, not tomorrow, and "the election does not change that", as one official puts it.

They have offered to train Iraqi military police, but only outside the country, possibly in Jordan or Qatar. They argue that they have already made a concession by writing off Iraqi debt, a move they originally resisted.

So what could they bring to the Brussels dining table? The Americans might hope for more robust French public support for the new Iraqi government to resonate in the Arab world. This could help to undermine the legitimacy of the insurgents. Yet the French want to retain the anti-American card on which so much of Mr Chirac's stature in the Arab world depends. They might be persuaded to tone down their calls for American troop withdrawal by the end of the year.

And in return? Above all, the French want Mr Bush to be seen to make a peace effort in the Middle East. This, they have long argued, not democracy in Iraq, is the key to bringing stability to the region. It now looks a more plausible hope. But with so much distrust, it would not take much in the coming weeks—disagreement over Iran, say, or on lifting the EU arms embargo on China, which France has pushed—to upset the relationship again.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Turkey's opposition

Time for a change

Feb 3rd 2005 | ANKARA
From The Economist print edition

A farcically out-of-touch party

Get article background

CONSPIRACY theories blaming the Americans for all that ails Turkey are not new, as Condoleezza Rice, America's secretary of state, may find when she visits Ankara this weekend. But when Deniz Baykal, leader of the opposition Republican People's Party, suggested that the Americans had orchestrated the latest challenge to his 12-year grip, even the crustiest anti-Americans laughed.

Reuters

Political debate, Turkish-style

Mr Baykal and his party have become objects of ridicule following a special convention to elect a new boss. Mr Baykal defeated Mustafa Sarigul, mayor of Istanbul's rich Sisli district, but only after a two-day slanging match that degenerated into a mob fight. Live television coverage of the mêlée showed rival supporters hurling chairs at each other. As Mr Baykal listed evidence of his challenger's alleged misdeeds, Mr Sarigul cleaved his way to the lectern to respond, punching a rival mayor on the way. “He also stuck his fingers in my mouth and bit me,” his victim claimed.

The party, better known by its initials CHP, was set up and led by modern Turkey's founding father, Kemal Ataturk, until his death in 1938. It has clung to his legacy, projecting itself, with the generals, as the guarantor of secularism in Turkey. As religiously conservative Anatolians migrated to the cities, the handful of pro-secular ideologues running the CHP remained oblivious to the changes in Turkish society, condemning themselves to political irrelevance.

Weakened by corruption scandals and internal feuds, the CHP failed in 1999 to muster the minimum 10% of the vote that is needed to win seats in parliament. Yet Mr Baykal, who is now 66, managed to hang on. In 2002 the CHP got back in with 19%, but that success looked puny against the 34% won by the mildly Islamist AK party that now governs Turkey. No other party

from either left or right was elected to parliament, leaving Mr Baykal as the single-handed opposition to the charismatic prime minister, Recep Tayyip Erdogan.

Last week's fiasco suggests that neither he nor his party is up to the task. With no other credible opposition in sight there is a dangerous political vacuum, which pessimists think can be filled only by the armed forces. Some hope that the European Union might be able to curb Mr Erdogan's occasional blunders, as happened when he tried to criminalise adultery last year. But many would agree that, in the interests of Turkish democracy, it is past time that the CHP reformed itself—and that Mr Baykal stepped down.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Charlemagne

Europe's dash for growth

Feb 3rd 2005
From The Economist print edition

The European Commission puts the economy first

JOSÉ MANUEL BARROSO, president of the European Commission, appears to be taking Bill Clinton as a role model. Like Mr Clinton, he began his term with a pointless and damaging row about homosexuality: although in his case, it was about alleged gay-bashing by a prospective European commissioner, not about gays in the military. Now Mr Barroso is trying to boil his programme down to something like the famous Clintonian slogan: “it's the economy, stupid.” Such candour is not allowed in official documents, however, so the programme that Mr Barroso presented on February 2nd was soporifically entitled “A partnership for growth and jobs”. But its central message was clear. The European Union's biggest problem is slow growth, and the Barroso commission wants to do something about it.

For a political leader to make creating prosperity his top priority would usually be utterly banal. But this is the EU, where Mr Barroso's statements have been greeted with deep suspicion. The left fear that he is intent on dismantling EU social and environmental legislation. Poul Nyrup Rasmussen, head of the party of European Socialists and a former Danish prime minister, even used the ultimate Brussels boo-word, accusing Mr Barroso of promoting a “neo-conservative” economic agenda. But economic liberals are also wary. They fear that a commission-sponsored “dash for growth” could degenerate into doomed and wasteful efforts to promote European industrial champions.

Both sets of fears focus on Günter Verheugen, a German who is a vice-president of the commission with special responsibility for competitiveness. He played a central role in drafting this week's document. Before Mr Barroso was even appointed, the German government made clear that it wanted a key economic portfolio in the commission. Inevitably, therefore, Mr Verheugen is seen as Berlin's man. His every statement is scrutinised for evidence that he is taking orders from the German government or from German industry. When Mr Verheugen suggested that merger rules might be applied less fiercely, liberals cried foul. When he spoke of the need to lessen the regulatory burden on industry, greens and trade unions bristled.

Mr Verheugen has also clashed fairly openly with some of his colleagues. On his desk this week stood a gorgeous bunch of red tulips: a peace offering from Neelie Kroes, the Dutch commissioner for competition, with whom Mr Verheugen has been squabbling. Mrs Kroes and her team are worried that the German commissioner may try to annex their powers over mergers and state aid. But to judge from Mr Verheugen's conversation, it is promoters of social and environmental legislation who should be more worried. He says that he wants his “personal trademark” to be a more aggressive approach to deregulation. Acknowledging that cutting red tape has long been a mantra for the commission, as for governments everywhere, he says, “I want to be the guy that really did it.”

Asked for an example of red tape that needs cutting, Mr Verheugen responds instantly: “REACH”. This is the acronym for an EU directive on chemicals, promoted energetically in the previous

commission by Margot Wallstrom, a Swede who was then environment commissioner. Mrs Wallstrom sought to demonstrate the need for stricter restrictions on chemicals by taking a blood test to show how many noxious substances had infiltrated her system. (Apparently, she is stuffed full of flame retardants, although she looks very well on it.) But Mr Verheugen is more interested in the impact of the directive on the health of European business. He complains that studies of the cost to industry of complying with REACH come up with figures ranging from *euro*2 billion ($2.5 billion) to *euro*40 billion. Whatever the right figure, Mr Verheugen considers it too high. He says that it is too late (and anyway undesirable) to withdraw the legislation entirely, but he hopes to see it amended to make it friendlier to industry. And from now on, he plans to ensure that all draft regulations coming out of the European Commission are subjected to a rigorous impact assessment, so that their costs are spelled out.

The delusion of champions

If slashing regulation was all that Mr Barroso and Mr Verheugen were about, economic liberals could relax, and even cheer. But there are less appealing ideas in the European air. The hoopla over the launch of Airbus's super-jumbo last month has given fresh heart to those who believe that governments can pick economic winners. Jacques Chirac, the French president, has talked of using Airbus as a model for a host of other industries, from telecoms to energy. *Le Monde*, the bible of the French establishment, has proclaimed “the return of industrial policy”, and has even fingered Mr Verheugen as its chief promoter within the European Commission.

The man himself seems eager to dispel any such impression. Airbus, he suggests, is a “misleading example”, because it operates in a unique industrial sector. He adds that “anyone arguing for a return to 1970s-style industrial policy would be very isolated within Europe.” Mr Verheugen is not opposed to the emergence of European champions. But he says they must be produced by the market. “I have told European industrialists they can come and see me any time, but there are two things they cannot ask for: money, and protection from competition.”

If all this can be taken at face value, it sounds good. But while there is no doubting the determination of the Barroso team to breathe new life into the European economy, most of what needs to be done is sadly not in their power. Structural reforms to Europe's welfare states and deregulation of labour markets remain largely the province of national governments. Still, if the commission shows more restraint when exercising its formidable powers over social, environmental and industrial legislation, it would at least be following the sage advice given to new doctors: “first, do no harm.”

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Anti-social behaviour

Enemies of the state?

Feb 3rd 2005 | SHEFFIELD
From The Economist print edition

People worry more about anti-social behaviour, but that's not necessarily because there's more of it about

Get article background

THE trouble began in Meersbrook, a district of the poor northern town of Sheffield, in the autumn of 2003. At first it was just a group of teenagers loitering outside a shop on the corner of Valley Road and Brooklyn Road. But their numbers grew, swelled by an unruly family that had recently moved in nearby. Walls were soon covered with graffiti, fireworks were let off in the street and drug dealers began to tout for customers. “For Sale” signs appeared on local houses. A neighbourhood that had never been particularly cohesive seemed about to fall apart.

Then, last August, the police secured a “dispersal order”, which enabled them to break up groups of loiterers and return under-16s to their homes. They also asked six local people to sign contracts promising not to misbehave. The contracts have no legal force, but seem to have worked. The graffiti have gone, the gang is smaller and better mannered and, as Steve Kidder, a local shopkeeper, puts it, “we're gradually getting back to where we were.”

Until recently, Sheffield's police would probably not have devoted so much energy to solving a neighbourhood problem. Their priorities—determined largely by the Home Office, 140 miles away in London—were tackling burglars, car thieves and other criminals who could be locked up for a satisfyingly long time. But priorities have changed and resources been redirected. Eighteen months ago, the local sergeant, Alan Boyle, had four officers to deploy in the area. He will soon have 20.

The change is a response to demand, partly from local people and partly from the government, for action against the kind of petty irritations collectively described as anti-social behaviour. Five years ago, the concept was almost unknown. These days, it is one of the most prominent issues in local and national politics and in the British press (see chart).

That is probably not because there is more of it about. Vandalism (the closest proxy for it in the statistics) has declined since the mid-1990s along with most other crimes. Rather, says Louise Casey, director of the government's anti-social-behaviour unit, public concern has migrated from old-fashioned things like burglary and car theft to petty incivilities. “As crime has fallen, it has opened up some spare capacity to worry about litter, graffiti and abandoned cars.”

The other reason more attention is paid to anti-social behaviour is that there are more tools for dealing with it. Most powerful of these is the anti-social behaviour order (ASBO)—a civil order, lasting for a minimum of two years, that can be used severely to restrict a person's liberties. In September 2003, a mentally unstable drunk, Paul Booker, was barred from doing anything “likely to cause harassment, alarm or distress” to anybody in Sheffield, or from using any bus, tram or train in South Yorkshire. Perhaps not surprisingly, he soon broke the order and was jailed.

In Sheffield, ASBOs are generally sought only after milder techniques have failed to change a person's behaviour. Just 49 have been handed out since 1999—one to a Meersbrook resident. That contrasts with other northern cities such as Manchester, where 20 orders are being handed out every month. There, according to Martin Lee, head of the council's nuisance strategy group, ASBOs are frequently used as an option of first resort, even for petty troublemakers. “If one person says ‘I was intimidated while using a cash machine,' then we're in.”

Manchester has used ASBOs against both minor indiscretions and serious crimes. Last year, it secured an order preventing four gang members from wearing body armour or riding pedal cycles. Such a move has two advantages over prosecuting people for criminal offences: it is easier to prove a breach, and the resulting sentence is likely to be tougher. In 2003, a prolific Cardiff shoplifter was caught stealing from two shops. For one of his crimes, he was sentenced to a month's detention—a standard tariff for a persistent offender. In entering the second shop, however, he breached the terms of an ASBO. For that, he was sentenced to 18 months in prison.

The government approves of Manchester's war on incivility. David Blunkett, the former home

secretary, viewed the number of ASBOs handed out as a vital measure of police performance; he also affirmed that they should not necessarily be regarded as a weapon of last resort. But is the tough approach the better one?

It is not yet known how many people stick to the terms of their order. Of the 855 ASBOs handed out in England and Wales between June 2000 and December 2002, just over a third—305—were breached in the same period. Not bad; but, since the minimum duration of an ASBO is two years, the proportion ultimately flouted will almost certainly be higher.

A more important test is what happens when the forces of law and order are deployed away from areas like Meersbrook, as eventually they must be. If the Home Office's predictions turn out to be right, locals will gain the confidence to deal with petty nuisances themselves. If, on the other hand, they come to believe that the only remedy for incivility lies in the police and the courts, they are likely to remain cowed.

So far, the drive against anti-social behaviour has encouraged some neighbourly behaviour. It has also given free rein to prejudices and suspicions. As Neil Pilkington, the chief solicitor of Salford City Council, puts it: “There are people in every community who believe that if you're under 18 and breathing, you ought to be on an ASBO.”

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Naughty children

Not just William

Feb 3rd 2005
From The Economist print edition

Anti-social behaviour used to be more acceptable, and more fun

IN A speech last year, Tony Blair traced the origins of anti-social behaviour to the 1960s. That decade, he explained, “spawned a group of young people who were brought up without parental discipline, without proper role models and without any sense of responsibility to or for others”. It's a widely held view. But if earlier generations were paragons of good behaviour, why do so many old children's books praise naughtiness?

Fiction aimed at pre-teenage boys contained especially poor role models. Among the most popular was Richmal Crompton's William, a well-meaning boy who is nonetheless drawn to trouble. William, whose adventures spanned the 1920s to the 1960s, escapes the tedium of parental control in the company of his gang, the Outlaws, with whom he schemes against the adult world. At one point he eats a neighbour's entire crop of prize peaches as well as destroying a greenhouse; at another, the Outlaws kidnap a baby and put it in a room with a bottle of paraffin—not Harry Potter's sort of thing.

More dubious still are the adventures described in C. Day Lewis's 1948 book “The Otterbury Incident”. This tells the story of a gang of school children who heroically thwart a counterfeiting operation. Nothing untoward there—except that the children are, by modern standards, heavily armed. The criminal offences for which they might be prosecuted, as accurately summarised by Inspector Brook in the final scene, include “carrying lethal weapons with intent to wound, breaking and entering, intimidation, assault and battery, shooting at certain fellow citizens and discharging rockets at same”. Yet there is no suggestion that they should avoid fireworks or air guns in future.

Diane Purkiss of Oxford University believes that rowdiness on such a scale would fall foul of most editors these days. It is not that modern children's literature is devoid of outlaws; rather, rebellious behaviour is either the result of inadequate upbringing or exists safely in the realm of fantasy. “Children don't get to raid people's dustbins any more, although they do sometimes have the power to change the world.”

Fictional children sometimes did both. The schoolboy heroes of Rudyard Kipling's “Stalky & Co.” are robust even by the standards of William and the Otterbury gang. Expert spitters and cat shooters, they scheme their way through school. It is excellent preparation for adult life. In the end, Stalky heads for India, where his deviousness and disregard for procedural niceties turn out to be just the trick for running the empire.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Company taxation

Sparks fly

Feb 3rd 2005
From The Economist print edition

M&S may be about to cut government revenues and please Brussels

MARKS & SPENCER is not thought of as a great innovator these days, but it may precipitate a huge change. On February 1st, M&S and Britain's Inland Revenue appeared before the European Court of Justice (ECJ) to argue over Britain's tax regulation on “group relief”, which allows companies to offset losses from one subsidiary against profits from another. If M&S wins the case, most EU countries, including Britain, will have to reform their corporate tax rules.

Britain allows firms to offset losses of subsidiaries in Britain, but not losses of subsidiaries abroad, against corporate profits. This, says M&S, is a breach of the EU treaty as it penalises overseas investment. It wants to be allowed to offset the losses of its French, Belgian and German subsidiaries between 1998 and 2001 against its profits at other outlets.

The government argues that it doesn't let British firms offset losses from foreign subsidiaries because it does not benefit from taxes on profits from foreign subsidiaries. They are taxed by the country in which they are based. Moreover, letting companies deduct their losses abroad would distort the internal market, as companies would offset losses in low-tax countries such as Estonia against profits in high-tax countries.

These problems would not occur if European corporate taxes were the same everywhere. The European Commission, which supports M&S in its suit, has tried for years to get EU governments to do that. About a decade ago the commission proposed to allow multinationals to consolidate profits across union borders, but it was never approved. When László Kovács, the new European commissioner for taxation and customs union, took office at the end of last year he said he was in favour of the creation of common consolidated corporate taxation.

But Britain's Treasury can count on support from Germany, Greece, France, the Netherlands, Ireland, Finland and Sweden, none of which permits the global consolidation of companies' profits. France lets only a handful of blue-chips including Vivendi, Total and Areva consolidate profits and losses of all their affiliates at home and abroad. Germany's system of *Organschaft* allows the consolidation of a group's profits for tax purposes at home, but the regulation does not apply across borders. Only Denmark, Austria and, more recently, Italy have introduced a system whereby companies can consolidate profits of their subsidiaries within the EU.

If M&S wins the case it hopes to gain at least £30m ($57m) in tax repayment. Even worse for the exchequer, almost 60 multinationals have brought a class-action suit at courts in Britain. If M&S wins, the exchequer might have to repay more than £1 billion in taxes to them. If other multinationals follow suit it could cost even more.

The government could abolish group relief altogether, but business wouldn't like it, for it would put British companies at a disadvantage and encourage them to move to fiscally friendlier places.

According to Christopher Morgan, head of European tax at KPMG, an audit firm, M&S is likely to win. Adam Craig, head of the EU tax practice at Deloitte, another auditor, thinks the outcome is less certain. What is clear is that the ECJ will take at least another year to reach its final decision. Having waited years for its day in court, M&S will have to be patient for a little longer.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Animal-rights extremists

Flat-earth fighters

Feb 3rd 2005
From The Economist print edition

New laws to catch people-haters face the same problem as the old ones

IF AWARDS were given for thinking up new ways to frighten people, Britain's animal-rights extremists would win lots of them. Their inventiveness and determination has frightened the government too. The prospect of losing pharmaceutical research business prodded the Department of Trade and Industry into announcing amendments to a crime bill this week. Their aim is to make it easier to catch the people who target suppliers to Huntingdon Life Sciences, a research firm in Cambridgeshire, or to Oxford University's proposed biomedical research facility. If found guilty, they will get a five-year sentence and a big fine.

The new proposal does at least target the right problem. Since the labs started going to court and taking restraining orders out on malicious campaigners, getting at suppliers has been a far more effective way to hurt their business. Injunctions cost money and take time, though, so companies who can find other clients are more likely to just cut their ties with labs and run. Last year 113 gave in, according to the Association of the British Pharmaceutical Industry. Making harassment of suppliers a criminal offence, rather than a civil one, could make it easier for victims to protect themselves.

“If any of this is enacted, you will have stronger laws than we do,” says Mary Hanley of the National Association for Biomedical Research in Washington, DC. In America, the law is still focused on protecting the labs themselves from attack. Increasingly, though, it is the people who have a commercial relationship with them who get harassed there too. Mrs Hanley cites the case of a man who did genetic tests on fruit, but was hounded after sending a sample off to a research centre that also used animals.

But the proposals do have shortcomings. First, they apply only to animal-rights extremism, and therefore flout the principle that good laws are ones with general applications. Second, they will not make it any easier to gather evidence on criminal activists, which is where the police are currently struggling.

“They are very forensically aware,” says a spokesman for the National Extremism Tactical Co-ordination Unit (NETCU). When protesting, or making home visits, animal-rights extremists wear disguises. They use untraceable e-mails to bring down computer systems. And they use only self-sealing envelopes. Collecting incriminating evidence from eyewitness reports, CCTV or DNA is therefore difficult, and convictions are rare.

Scientists hope the law will allow them to get on with their work undisturbed, but this is probably optimistic. “The government is not going to propose something that is not going to work,” says the Research Defence Society, with touching faith. But there is, at least, more solid comfort in a promise by the science minister, Lord Sainsbury, that the government will help out Oxford University with some of the security costs of building its lab.

Private education

Breaking in

Feb 3rd 2005
From The Economist print edition

Britain's cash-strapped universities face private competition

Get article background

STATE-FINANCED universities have plenty to complain about. The subsidy trough is never full enough, and political meddling is a constant nuisance. But now there's a new and much more fundamental threat: private competition.

The first news is that BPP, a for-profit provider of professional training, has passed an important mark in its attempt to become a university. The Privy Council, a feudal relic that regulates such things, has asked the Quality Assurance Agency, which polices standards in higher education, to start a full inspection of BPP.

If all goes well—which it should, as BPP's pricey courses are generally regarded as being of higher quality than many public-sector universities—the company could gain degree-awarding powers in about 18 months. That would then allow it to offer masters' degrees in subjects such as law, finance and banking, to go with the professional qualifications for lawyers, accountants, actuaries and the like that it currently teaches. Financial Training, BPP's main rival, is considering a similar step.

That would be a big competitive threat for the existing universities, in particular in the deregulated post-graduate and overseas student markets, on which most depend for profits to subsidise the loss-making business of teaching British undergraduates.

The other news is that two universities, Buckingham and Brunel, are in talks to set up a new graduate medical school, opening in 2008, for 200 students ready to pay around £20,000 a year.

Such a move would bring onshore a business that has enriched foreign entrepreneurs. Britain's state-subsidised medical schools are hugely oversubscribed: in the graduate market, at which the new venture is aimed, the chance of gaining a place is only one in five. So would-be doctors have been going abroad in increasing numbers, chiefly to the Caribbean and eastern Europe. Doctors graduating from any medical school recognised by the World Health Organisation may—in theory at least, and provided they pass a qualifying test—apply for jobs in the developed world.

Already some small independent outfits are teaching students overseas courses in London. But Balraj Sidhu, who runs the London College of Medicine, which teaches offshore courses, says that the business is “infested by charlatans” and that much of the teaching is “dreadful”. The Cambridge end of a Ugandan medical school went bust last year; its students ended up sleeping in a park.

Brunel and Buckingham will have an advantage: their graduates will be able to practise in Britain

without further ado. They will also, officials say, be eligible for the same £10,000 annual subsidy for hands-on hospital training that graduates from state-funded medical schools receive. Students from offshore private schools pay NHS hospitals handsomely for that.

The two universities had spotted the gap in the market independently: Britain is expected to be short of 25,000 doctors by 2022, according to an official estimate. Combining forces–which both institutions' vice-chancellors favour—will create a much more powerful contender. Buckingham has already recruited Karol Sikora, a top cancer specialist, as dean. Now the search is for donors and investors in the school.

Existing medical schools (and indeed other university departments) may now start wondering why they don't charge rich students more too. That is a subversive thought, as the planned economy of Britain's higher education system frays.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Wind farms

Breezy

Feb 3rd 2005
From The Economist print edition

Plans for wind farms multiply faster than evidence that they work

BRITAIN is top of a previously unknown league: countries in which to invest profitably in wind farms, according to Ernst & Young, an accountancy firm. As a result, wind farms are spreading across the country like warm butter.

According to a study by *Platts Power UK*, a specialist energy magazine, 21 gigawatts (GW) of large renewable power projects are being planned for the next five years. Britain currently has about 1GW installed now, with an extra 2.5GW either being built or awaiting construction in the next 12 months. If all the projects that are in the planning system now—plus all those that are being plotted but have not yet made it to planning—are built, this would mean about 200 extra wind farms, according to Dominic Maclaine of *Platts*.

Though this is unlikely to happen, as many schemes won't get planning permission and others will

not get the necessary funding, the *Platts* report does highlight a problem in the way the pseudo-market is set up. Wind farms get one Renewable Obligation Certificate (ROC) for each megawatt-hour they generate. Power-distribution companies then buy them, or face fines for failing to buy a set proportion of renewable energy every year. If all this capacity were to be built, the ROCs would lose around a quarter of their value. That's because they hold their value only if there are not enough of them to go round.

The quirks of the ROCs market are just a distraction when compared with the other problems that advocates of wind power face, though. The evidence from countries like Germany and Denmark, where wind power has been tried on a larger scale, is not encouraging. A report by E.ON Netz, which runs part of Germany's electricity grid, found that over the course of 2003 the juice from wind farms amounted to only a sixth of their installed capacity. That's mostly because wind power is hard to forecast. If the forecast differs from the actual generation, the shortfall must be met by using reserve capacity. Conversely, there's no way to store excess electricity when the wind blows unexpectedly hard.

A second problem comes from increasingly vocal resistance to wind farms from local campaigners. People such as John Constable, an English literature don at Cambridge University, who knows lots about the mathematical differences between poetry and prose, can make formidable opponents. Mr Constable started investigating the viability of wind farms when one was proposed near his house. Now he is research director for the Renewable Energy Foundation, which takes a sceptical attitude towards wind power. Groups such as Highlands Before Pylons, which worries about the big pylons needed to connect new turbines to the power grid, have also multiplied, and are determined to get Britain demoted from the top spot.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Welfare reform

Off the sick

Feb 3rd 2005
From The Economist print edition

The government is treading carefully in its attempt to reform incapacity benefit

THE government is planning another stab at welfare reform. The particular problem Tony Blair wants to address is the 2.7m people who claim incapacity benefit at a cost of about £12 billion a year. Mr Blair claims it's not just about saving money by cracking down on scroungers, but about providing better incentives for people to rejoin the workforce, which is good for them as well as for the taxpayer.

Estimates vary about how many of these people might be cajoled or encouraged back to work. According to Alan Johnson, the work and pensions secretary who published his department's five-year plan on February 2nd, a million recipients of the benefit say they would work if given the chance. David Willetts, his Tory shadow, says that only one-third of claimants have medical conditions so severe that work of any kind is beyond them.

Mr Willetts also points out that there are 159,000 people aged under 25 on the benefit—a 60% increase since Labour came to office in 1997. This conveniently deflects attention from the fact that, when last in office, the Tories surreptitiously moved lots of long-term unemployed industrial workers on to the benefit as a way of massaging down the jobless figures.

Since 1995, despite rapidly rising employment, there has been little change in the number of claimants. The government thinks that the current system gives people who may initially have genuine health problems a perverse incentive to remain on benefits indefinitely. Once someone has been “on the sick” for more than 12 months, their benefit rises from £56 to £74 and little is done to check up on their condition or help them back to work.

Mr Johnson, who laments the waste of human potential caused by the present system, proposes that claimants should be divided between those who really are too sick to work and those who, with the right mix of incentives, might become capable of earning a living again.

To that end, he wants doctors to focus on advising patients how to manage their ailments so they can work, instead of protecting them from work as they do now. Within three months, each claimant would be subject to a personal capability assessment which would determine their future employability and what kind of support they need to return to work. Those who really can't work will get more benefit than now while the others will get an allowance if they co-operate with attempts to find them employment. People who break the rules will lose money.

But the new scheme is neither radical nor practical. For a start, it will not come into operation until 2008 and, even more puzzlingly, existing claimants will be left alone if that's what they want. Frank Field, a Labour MP who was briefly minister for welfare reform in Mr Blair's first government, also argues that dividing “sheep from goats” will be hard. He proposes flat-rate benefit for all unemployed people, regardless of invalidity.

But Mr Blair and Mr Johnson are mindful of the rebellion by 67 MPs in 1999 when Labour last tried to tackle disability benefits. They are keen to avoid demonstrations by protesters in wheelchairs.

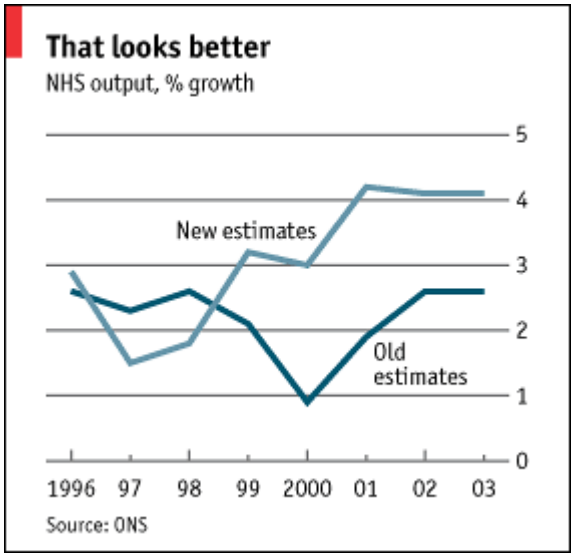
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Public services

Never mind costs, feel the quality

Feb 3rd 2005
From The Economist print edition

New ways of calculating government output will be politically controversial



A KEEN interest in the precise way that GDP is measured is usually confined to official number-crunchers and nerdy economists. But when the numbers in the national accounts started to pose awkward questions about whether Labour's big spending spree was delivering value for money, ministers started to take a keen interest. Sir Tony Atkinson, an economist at Oxford University, was asked to investigate why government productivity appeared to be plummeting.

Sir Tony's report, unveiled on January 31st, presages a big shake-up in the way that government output and productivity are measured. Already, the review has prompted new estimates of NHS output which have raised its growth in recent years compared with previous figures (see chart). Schools are next in line. By the end of April, the Office for National Statistics (ONS) is likely to release figures indicating the impact of changes to educational output. Since that could be just days before a general election, the statistics may become mired in political controversy.

The issue that Sir Tony has been grappling with is how the output of the public services—worth a fifth of GDP—should be estimated. Until 1998, the ONS followed the rule that output was equal to real inputs. This method implied that the efficiency with which the public services turned inputs into output remained constant. However, the ONS now makes direct estimates covering over 60% of government output, which has opened up the potential for productivity to grow or to fall.

Embarrassingly for Labour ministers, the new official figures have shown declining rather than rising productivity in the public services. Yet this could reflect weaknesses in the methods being

used to measure output rather than poor value for money. For example, the output of schools is based on a pupil count, so that productivity falls when there are more teachers, even though this cuts class sizes.

Faced with such knotty difficulties, one response might be to revert to the former method of using inputs to measure government output. After all, America still uses this approach. However, this is not an option open to the ONS, since direct measures have to be used by almost all countries in the European Union by 2007.

But if the ONS cannot go back, going forward will nonetheless be tricky. Sir Tony insists that the output of the public services must take account of changes in quality. In principle, this seems incontestable, but establishing estimates that are generally accepted will be hard.

In any case, the ONS still has its work cut out to make less controversial but essential improvements. For example, its series for NHS output assumes that it is growing throughout Britain at the same rate as in England, which is questionable. The figures for visits to family doctors are shaky. Another worry is about the “reference-cost” figures for various types of treatment, which are the main new source for the revised output series. These should be reconcilable with hospital accounts, but this is not the case for a third of acute-care trusts, according to the Audit Commission.

Even when the ONS has tackled such deficiencies, doubts will remain about basing government output on figures also being used to monitor performance in the public services. “There is the potential for Soviet-style distortions,” says Nicholas Oulton of the London School of Economics. “The people supposed to be objective providers of information like hospital administrators are being judged on it.” The more glowing the picture that the new numbers paint, the less likely it is that anyone will believe them.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Bagehot

Blairism triumphs, Gordon waits

Feb 3rd 2005
From The Economist print edition

The Blairites are on a roll, but for how long?

Get article background

BLAIRISM is in the ascendant. The departmental five-year plans rolling off the government's presses are all impeccably on-message. The latest—from the Department for Work and Pensions—is not a page-turner, but the men at Number 10 think it a fine work, for it offers further proof that the prime minister has succeeded in wresting control of the domestic agenda from Gordon Brown, the chancellor of the exchequer, in the past year.

The DWP has traditionally been a fiefdom of the Treasury. But since the departure in September of Andrew Smith, one of the chancellor's most faithful acolytes, it is no longer under Mr Brown's sole authority. The department is now being run by Alan Johnson, the quiet, skilful former higher education minister who successfully steered Mr Blair's policy of raising tuition fees for university students past bitter Labour Party opposition. But the determination to tackle Britain's pensions mess and change the incapacity benefit rules comes directly from Number 10. All sorts of Blairite ideas, linked by the common theme of making public services more responsive to individual needs by extending competition through quasi-markets, will pack the Labour Party's election manifesto.

Yet for all the fervour and optimism of the Blairite believers, the whole enterprise has a distinctly fragile feel to it. Partly, that is because the group of people responsible for driving it—a sprinkling of Downing Street advisers and a handful of ministers—is so tiny. But mostly, it is because of the lurking presence of Mr Brown. Mr Blair's recovery of zest and confidence last summer has given his people the chance to finish the job. But the time available has been limited by his promise to quit within four years of the election, the fear that he may go rather sooner and the near-certainty that Mr Brown will succeed him.

Governments naturally tend to fret that their good work will be undone if they lose an election and the other lot gets in. With the Blairites, though, the worry is not about what happens if they lose the next election but what happens if Labour stays in power after Mr Blair has gone. That's because the “other lot” happens to be sitting at the cabinet table.

As might be expected, the Blairite vanguard maintains that such fears are overdone, and makes a fairly plausible case. First of all, say Mr Blair's advisers, big reforms are always driven by a small number of people in government. That was certainly true of the Thatcherite microeconomic reforms of the 1980s. And once it was widely accepted that they had transformed the economy's performance, reversing them became unthinkable.

The Blairites argue that public-service reform is now making a difference, and that people have noticed. Since the introduction of independent treatment centres in 2002, the NHS has paid for eight times as many cataract operations. A few weeks ago, Wales's health minister was sacked

because the unreformed Welsh NHS had failed to match the progress of the English NHS.

In the past Mr Brown's supporters have complained that Number 10 imposes its views without first preparing the ground. The departmental five-year plans are the Blairites' answer to that charge. Drawing up the plans has also helped commit ministers and civil servants to them. Downing Street insiders say that's important: “A thousand decisions have to be taken at department level to support each reform.” By getting ministers to present their plans to cabinet, Mr Blair has ensured that rows get resolved long before the manifesto is drafted. What's more, Mr Brown's objections carry less weight in cabinet than they do in private. Growing cadres of New Labour ministers and MPs are champing at the bit to carry things forward.

As for Mr Blair's political longevity, the Blairites argue that four years is quite a long time and that the power he derives from patronage will begin to dissipate only after he carries out his last ministerial reshuffle. Nor should there be that much change once Mr Brown gets the job. The personal rivalry between the two has exaggerated the ideological differences between them, and Mr Brown will not want to define himself by trying to reverse successful reforms. A former adviser to Mr Blair says: “The genie is out of the bottle and Gordon won't be able to put it back.”

When the torch passes

Plausible? Certainly. Convincing? Not entirely. The claim that Mr Brown's lack of enthusiasm for injecting market disciplines into public services is just a pose dictated by his determination always to seem a bit to the left of the prime minister—“Gordon's 10% game” as it has become known—is too complacent. As “Brown's Britain”, Robert Peston's semi-authorised biography, makes clear, when Mr Brown evaluates any new policy, the key test for him is whether it is likely to advance equity.

Mr Brown appears to think that the changes taking place in the NHS are analogous to what has happened to dentistry in England: bringing in private operators may increase capacity quickly, but it may also create a two-tier service. He does not believe that a market can be efficient when patients have much less information than health-care providers. Mr Brown may be wrong, but his criticisms are not trivial. If, as prime minister, he concludes that public-service reform has taken a wrong turn, why would he not want to do something about it?

Power is also likely to drain away from Mr Blair long before his last reshuffle. Political advisers work for just one master, but ministers are different. As long as they reckon Mr Brown has no serious challenger they will become ever more reluctant to expose themselves to his disapproval.

The command and the zeal of the Blairites are not in question at present, but at some point both will be tempered by the pressure to unite under a new leader. And that time is likely to come sooner than they expect.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Corporate mergers

The fall of a corporate queen

Feb 3rd 2005
From The Economist print edition

AT&T, once one of the world's greatest companies, loses its independence

FROM the very first words spoken over a telephone in 1876 by its inventor Alexander Graham Bell—"Mr Watson, come here, I want to see you!"—AT&T always wanted to have its own way. And for much of its 128-year history, the American Telephone & Telegraph Company got it. First, as a brash start-up that won over 600 patent lawsuits in its first 18 years, then as a cut-throat competitor that pushed the limits of lawfulness to consolidate America's telecoms market and finally, until 1984, as a government-sanctioned monopoly.

But the modern era has been less generous, as the business behind AT&T's central activity of connecting long-distance calls crumbled. This week, SBC, one of the "baby bells" that was spun out of the company as part of a court-ordered break-up in 1984, acquired "Ma Bell", as AT&T is known, for around $16 billion, ending its reign as an independent firm. The new owner may yet adopt the famous brand as its corporate name. But the firm born in the 19th century, and which dominated the 20th, failed to survive long into the 21st.

The deal creates America's largest telecoms firm, with combined revenues of $70 billion and 210,000 employees (of which 10% are to be cut). AT&T had been for sale for a while, and had slashed debt and staff to pretty itself for suitors. SBC gets to sell to AT&T's millions of corporate customers sophisticated data and voice services—around $20 billion of AT&T's revenues. The deal may prompt further consolidation (MCI is fingered as the next target by three other Bell companies, Qwest, Verizon and BellSouth), now that the period of internal rebuilding by telecoms firms after the bubble burst in 2000 is over.

Ask not for whom the Bell tolls

For much of the past century AT&T was the envy of the corporate world—the largest firm on the planet both by revenue and market capitalisation. No share was more widely held—the firm was so solid it was considered ideal for “widows and orphans”. Its legendary research arm, Bell Laboratories, was responsible for some of the 20th century's greatest inventions, from the transistor to the laser, and fielded seven Nobel Prize winners. At the time of the break-up in 1984 AT&T boasted around 1m employees. So what went wrong?

In short, the industry changed but AT&T failed to change with it. A century-old ethos of public service and reliability—thanks in part to its cosseted life as a protected monopoly with regulated rates—was ill-suited to competition in a world in which new technology cut the cost of calls and lowered rivals' barriers to entry. Despite owning the world's foremost corporate research lab, it missed moving into new technologies such as wireless and the internet that would become the cornerstone of modern communications.

“It is a tragic fall and I lament the passing, because it was a huge disruptive success in its day”, says Clayton Christensen of Harvard Business School, author of the best-selling “Innovator's Dilemma”. “The world is filled with companies that are marvellously innovative from a technical point of view, but completely unable to innovate on a business model.” In the early 1980s, AT&T negotiated an antitrust settlement with the Department of Justice to separate its long-distance operation and create seven local telephone firms, spread across different regions. “AT&T will now be free”, gushed *The Economist*, to put a computer on every desk connected by “broader-band links” and “pocket-mobile telephones in big cities”. Yet at three critical junctures over the past two decades—involving wireless, computing and cable—the company misplayed its hand.

First, AT&T underestimated how important wireless communications would become. At the time of the break-up in 1984, AT&T relied on a report by McKinsey, a consultancy, that claimed there would be fewer than 1m wireless phone users by 2000. In fact, there were 740m. Cellular technology was then spotty—calls were often lost, the signal short and the power used by devices high—so AT&T declined to enter this small market. Until, that is, 1994, when it paid $11.5 billion for McCaw Cellular, which became AT&T Wireless and was sold last year for $41 billion.

The second stumble was in computing. After the break-up, AT&T expected to become a powerhouse in computers. Shedding the slow-moving local operators and retaining the Western Electric equipment business seemed a brilliant result from the antitrust process. AT&T even bought a computer maker, NCR, in 1991. But the fast-paced computing industry did not suit the stodgy former monopolist. And the equipment arm struggled because local operators declined to rely on a single supplier and gave half their business to other firms.

So, in 1995, AT&T voluntarily broke itself up still further, shedding Lucent, its re-named equipment maker, and NCR, at a huge financial loss. Now the downsized AT&T would focus on services.

This was the dawn of the commercial internet, yet AT&T was nowhere. Two decades earlier it had dismissed the technology as unworkable, and later, as too small a market. It had even rejected numerous requests from American officials over three decades to operate the internet backbone. Just as by inventing the transistor AT&T unleashed one of the central forces in technology that would eventually undermine the company, so it also missed the potential of the internet despite it running over its long-distance lines. In the 1970s, Bell Labs developed the UNIX computer operating system, which (evolved by others) still powers most of the world's large corporate computers. Alas, at that time AT&T was prevented by regulators from moving into computing, so UNIX was commercialised by others.

The third big mistake was to buy cable operators in the late 1990s. This was the right strategy at the wrong time and for too much money. At the height of the tech boom, AT&T's then boss, Michael Armstrong, paid over $100 billion for two cable firms, TCI and MediaOne. AT&T realised it needed direct access to consumers, as it could no longer count on the regional bells, now moving into long-distance after the 1996 Telecom Act opened up competition in the sector. But the cable infrastructure required costly upgrades, and Ma Bell's domineering ways clashed with the cable firms' culture of co-operation.

Barely a year later, as the stockmarket turned on telecoms firms, AT&T faced a debt crisis. It had to abandon the firms it had just bought, and with them, the strategy of offering a basket of communications services including voice, TV and internet access—a strategy now regarded as the likeliest way to succeed.

“The main lesson is that it is very hard to change a culture that has evolved for a particular type of environment,” says Andrew Odlyzko, a former Bell Labs researcher now at the University of Minnesota. AT&T grew up believing that communications comprised voice calls charged by the minute and the distance. But data subsumed voice, web traffic burst through the network via always-on broadband connections and distance is dead.

Is there a silver lining to this sorry tale? “It ought to be humbling to any empire-builder to see what was once the greatest corporation in America be acquired by one of its offspring”, says Paul Starr, a communications historian at Princeton University. “But it's not necessarily a bad thing when the mighty lose sleep at night.”

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Indian business

A splitting headache

Feb 3rd 2005 | DELHI
From The Economist print edition

A family row seems likely to break up India's biggest business group

RELIANCE, India's largest business group, is likely to be split in two later this year. That is the current forecast not only of many Indian bankers and analysts but also of the two camps representing Reliance's warring brothers, Mukesh Ambani, 47, who controls the group, and his younger brother, Anil, 45, who is trying to secure his share not only of the family's fortune but of management control. Since November 18th, when Mukesh made a startling and apparently off-the-cuff remark to a TV channel about differences over "ownership issues", the brothers have brought into the open a personal war that has been simmering in private for more than two years.

Indian newspapers have been carrying front-page stories on the fight for weeks. Many of these have been based on leaks—apparently from Anil's camp—about Mukesh's alleged corporate-governance misdeeds in Reliance Industries (RIL), the group's main quoted company, and in Reliance Infocomm, a telecoms offshoot. As chairman of both RIL and Infocomm, Mukesh has been criticised for rewarding himself with a chunk of equity worth about $1 billion, for granting himself and his wife Nita a 40.5% stake in Infocomm at a fraction of its value, and for boosting Infocomm's cash flows by getting RIL to inject $1.8 billion in preference shares on unfavourable terms. Mukesh has now returned the equity and referred the preference share issue to a board committee, while denying that the 40.5% share valuation was unfair. But the leaks continue.

Anil's aim appears to be to embarrass Mukesh to the point where he agrees to split the business empire on favourable terms. Anil's role in the group was reduced last year when he lost control of finance and media relations. He now only directly runs Reliance Energy, a power firm. He is said to fear that, should Mukesh die suddenly, control would go to Nita, not to him.

Founded in 1959 by Dhirubhai Ambani, the brothers' father, who died in July 2002, RIL made profits of $1.2 billion on revenues of $12.8 billion in 2003-04. So far, the row does not seem to have hurt performance—profits after tax were up by 52% in the quarter to December 31st—although rival bosses say that the firm has lost its air of invincibility, which until now has given it influence with politicians and bureaucrats, and has often frightened competitors.

The group's market capitalisation is $17.2 billion, so Anil would not end up poor however it is divided. But his demand for management control of leading group companies, rather than a cash pay-off, will be hard to meet. RIL is vertically integrated. Mukesh secured a board resolution in December that it should not be "dismembered".

K.V. Kamath, chief executive of ICICI, a leading Mumbai bank, and an old friend of the family, is currently assessing the value of all the group's holdings and the family's wealth on behalf of Kokilaben Ambani, Dhirubhai's widow. She will then try to broker a deal with her sons, to stop the row either going to court, or becoming so scandalous that India's stockmarket and company regulators feel obliged to intervene.

European business subsidies

Neelie ventures forth

Feb 3rd 2005
From The Economist print edition

A new crusade against state aid

AP

Neelie is very Kroes

IT WAS inevitable that Neelie Kroes, the European Union's new competition commissioner, would soon have her first big confrontation with France. Last week she sent Hervé Gaymard, France's finance minister, a letter full of reproach about France's failure to stick to the terms of last year's €2 billion ($2.4 billion) bailout of Alstom, an ailing state-owned engineering group. Then she increased the pressure by threatening to take the French government to the European Court of Justice (ECJ). On February 1st she met a member of Mr Gaymard's team who, hoping to avoid a lawsuit, said that his government would fulfil its obligations as soon as possible.

The commission says that the French government failed to meet commitments it made in return for the approval of its rescue package. It has missed two deadlines and done nothing to open the market for rolling stock. Nor has it implemented yet an EU directive on public procurement in transport.

Alstom will provide a tough test of Ms Kroes's determination to launch a sweeping reform of state-aid rules. She is working on a proposal to give European firms less but better state aid, with a focus on the EU's poorest countries. Her plan is to shift the focus of aid to research and innovation and to the promotion of small and medium-sized companies. She is especially critical of the use of bailout packages for big companies in rich countries, such as Alitalia, Italy's struggling airline, or Alstom.

The details of her proposals are not yet public, but some states are already up in arms about what they think she plans to do. Britain, France, Germany and Austria have sent Ms Kroes letters warning that her proposal would hurt jobs and drive investment abroad. Germany is worried about aid for companies in the former East Germany. Patricia Hewitt, Britain's trade minister, notes in her letter the risk that high aid differentials between the EU's regions could incite companies to relocate.

On February 1st an advocate-general of the ECJ, whose decisions tend to be followed by the court's judges, found that the Greek government's €194m aid package to Olympic Airways, the country's struggling airline, was illegal and should be repaid. If Ms Kroes sticks to her tough line, Alstom may well provide the court's next big case.

Europe's defence industry

The China syndrome

Feb 3rd 2005
From The Economist print edition

Lifting Europe's embargo on arms sales to China could hurt its defence industry

AP

Especially if you are Chinese

YOU cannot get much more patriotic than the American president's taxi. Pretty soon George Bush will be ferried around not in an all-American Sikorsky helicopter, but in a new Agusta US101. The new presidential choppers will be assembled in America by Lockheed Martin, but they are basically a product developed by an arm of Finmeccanica, a state-owned Italian defence conglomerate. Given Italy's support for the Iraq invasion, the country is evidently being forgiven for being European. The contract, worth just over $6 billion, was announced by the US Navy at the end of last week.

The deal caused a predictable flurry of protest in Congress, long used to pork being dealt out to purely domestic defence contractors. Europeans should have been cock-a-hoop, given that EADS (European Aeronautic Defence and Space company) is in the running to supply some of the 500 or so air-refuelling tankers that the Americans will soon need. The Europeans have an advantage because of the too-cosy relationship between Boeing's then finance director and a Pentagon official, both of whom have been convicted of improper dealings. The official was shown to have done Boeing favours, including leaking the price of a rival Airbus product.

But the real reason why Airbus, a subsidiary of EADS, in collaboration with either Lockheed Martin or Northrop Grumman (talks are under way with both), will get a slice of the lucrative tanker contracts once they eventually come along is that the US Air Force cannot risk having its entire fleet of tankers of one aircraft type. If a technical fault were to emerge, the world's policeman would be grounded. The existing fleet consists of converted civil jets made by Boeing, McDonnell Douglas and Lockheed. Lockheed is out of the civil-jet business and McDonnell has been absorbed into Boeing. The only alternative supplier is Airbus.

But all such logic is threatened by the political uproar that is sure to come when the European

Union lifts its sanctions against selling arms to China. Congress will not want tax dollars spent on European products and will resist technology transfers that could help the Chinese if Europe sells them warplanes.

BAE Systems, a British defence contractor with a huge presence in America (24,000 employees and sales of over $5 billion), is extremely worried about the side-effects of lifting the Chinese embargo. The French have led the effort to get the embargo lifted, in the hope of selling Dassault fighters and of persuading the Chinese government to allow Chinese airlines to buy Airbus passenger jets. With the embargo set to be removed by the end of June, the Chinese ended restrictions last week on orders for Airbus's big new A380 aircraft, which desperately needs business from Asian carriers.

So the French rush to get into the Chinese defence market could stymie European ambitions in America—roughly half the global market for advanced military equipment such as aircraft and missiles. But the impact could be far bigger, according to the boss of one leading American defence company: “It will push America and Europe in different directions, leading to a fortress US and a fortress Europe mentality.” The effect will be “chilling” for the co-operative transatlantic deals that Boeing and Lockheed have tried to forge with the likes of BAE and EADS.

BAE has renewed its efforts to expand further in America in the past year. But now it may be forced to turn back to Europe for partners—at an unfortunate moment. The incoming co-chief executive of EADS, Noel Forgeard (the man behind Airbus's recent success), is set on buying Thales, a French defence firm with a big presence in Britain, to turn EADS into a full-range defence contractor to rival BAE.

Mr Forgeard is a wily character who got the top job at EADS with the help of the French president (his former boss, when he was a civil servant) and without the full board being consulted, according to company sources. Having run rings round Boeing, he is perfectly capable of stitching up BAE by limiting its American ambitions, even if EADS itself suffers some collateral damage. If lifting the Chinese embargo stops BAE continuing as an Atlantic bridge, will it opt to join Fortress Europe, or instead become 100% American?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Fear of China

I spy spies

Feb 3rd 2005 | HONG KONG
From The Economist print edition

American politicians are attacking IBM's big Chinese deal

NOTHING gets a politician's juices flowing like a good scare story. Following the decline of offshoring as a hot issue on the stump, America's Republicans have latched on to a new one: national security. After taking “our” jobs, is China now sending us its spies?

Three senior Republican Congressmen are lobbying against the proposed $1.75 billion purchase of IBM's personal-computer business by Lenovo, China's largest PC maker. They claim that it will allow the Chinese government to acquire sensitive American technology and, potentially, use IBM's facilities to spy for the Chinese armed forces. In a letter to the treasury secretary, John Snow, the trio wrote that the deal “may transfer advanced US technology and corporate assets to the Chinese government”. Lenovo's parent company was founded, and is still controlled, by the Chinese Academy of Science.

On January 28th, the Committee on Foreign Investment in the United States, which examines national security aspects of corporate sales to foreign buyers, extended its routine 30-day investigation into the deal to a more thorough one that will take 45 more days. Most experts still expect the panel to clear the deal, perhaps with modest changes to the terms. But a surprise is possible. In 2003, the committee objected to Hong Kong's Hutchison Whampoa buying a stake in Global Crossing, a telecoms provider. In 1999, it blocked a Chinese-led consortium from acquiring $450m-worth of satellite assets.

The national security argument put forward by the three Republicans is hard to take seriously. Certainly China has little respect for intellectual property. Huawei Technologies, China's leading telecoms-equipment maker, was successfully sued by Cisco for intellectual-property theft in an American court. Chinese car firms counterfeit foreign models—one local favourite is half Mercedes, half BMW. The next Harry Potter books are out in China—though the real author has not written them yet. China is especially keen on advanced technology. Despite putting a man into space, China has a low-tech economy. Some 85% of the high-tech goods produced there are controlled by foreign firms. China consistently runs a $10 billion-plus annual trade deficit in technology.

But the PC and laptop operations that Lenovo is trying to buy from IBM are mature technologies with no clever applications and no real military use. As William Reinsch at the National Foreign Trade Council told the media, “the assets are low-tech, ubiquitous, and the Chinese have this technology anyway.” Although IBM invented the PC, “all the smart bits are provided by Intel and Microsoft these days,” notes Johnny Chan, an analyst at J.P. Morgan. IBM is selling its PC business because it is declining and barely profitable. True, it has some contracts to supply the American government. But if the committee believes that this leaves the country open to counter-intelligence, it can always insist that they are excluded.

In truth, the fuss over the Lenovo and IBM deal says more about Republican attempts to reverse

the relatively liberal attitude that America took towards China during the Clinton years than genuine national-security fears. As such, the agitated congressmen reflect a real fear of China's growing economic clout, twinned with an uncertainty about its political direction. One of the three Republican objectors, Donald Manzullo, said this week that Lenovo, as a state-owned Chinese company with no requirement to make a profit, “threatens America's economic security”. Since the group “already dominates the Chinese market”, it would surely “come in and try to dominate the US market as well”.

But even that claim is wrong. Far from “dominating” the Chinese market, Lenovo's 27% share and its margins are being squeezed by competition from America's Dell and Hewlett-Packard at the top end and by cheap unbranded machines from local rivals at the bottom. No wonder Lenovo's boss, Yang Yuanqing, complained recently that “the IT market in China is a battlefield”. As its finance director, Mary Ma, concedes: “If we just focus on China we cannot generate returns for our shareholders.” Perhaps it really is IBM's sales that Lenovo wants, not its information.

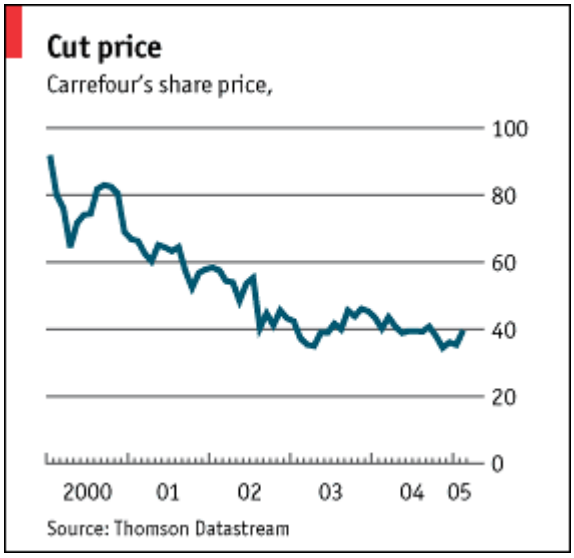
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Retailing

Changing shopkeepers

Feb 3rd 2005 | PARIS
From The Economist print edition

A new boss for Carrefour



DANIEL BERNARD, boss of Carrefour, the world's second-biggest retailer, was widely expected to be replaced at an emergency board meeting taking place as *The Economist* went to press. In a week of change at the top of French retailing, a day earlier Pinault-Printemps-Redoute (PPR), a retail and luxury conglomerate, announced the departure of its chief executive, Serge Weinberg. But whereas Mr Weinberg is leaving his company on good terms, Mr Bernard has been involved in long, acrimonious battles behind the scenes.

For months rumours have swirled around Mr Bernard. In particular, the Halley family, Carrefour's largest shareholder, has become dissatisfied with Mr Bernard's management. In each of the past five years Carrefour has lost market share to Auchan and Leclerc, its two big domestic rivals, and to deep-discounters such as Germany's Aldi. Carrefour's share price has fallen by 11% since September 2002, even as the CAC 40, the French stockmarket index, rose by 17%. Speculation has been rife about a possible takeover by Wal-Mart, the biggest retailer in the world, or by Britain's Tesco.

Mr Bernard was quite a success earlier in his 13-year reign at Carrefour. He drove the group's international expansion which transformed Carrefour into the main global rival to Wal-Mart. He also masterminded a merger in 1999 with Promodès, a French retailer founded by the Halleys. He continued to believe in his strategy. Only last week he talked to analysts about his plans to revive Carrefour, including €200m ($260m) in cost cuts and a store refurbishment programme.

Yet the financial markets reacted positively to news of his impending departure. His job is likely to be divided between two Carrefour veterans: José- Luis Duran may become chief executive and Luc Vandevelde (not long ago the rather ineffective boss of Marks & Spencer, a struggling British retailer), the Halleys' representative on Carrefour's board, the chairman. Mr Vandevelde's appointment would be a particular blow to Mr Bernard, for the two men clashed often in the past few months. The firm urgently needs a turnaround strategy. That will not be easy to find.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Face value

Lord of the rings

Feb 3rd 2005
From The Economist print edition

Rex

Can Cirque du Soleil's Guy Laliberté keep his circus business flying high?

BACK in 1980 Guy Laliberté was a street performer with a pair of stilts and a fire-breathing act. Today a talent for juggling and highwire balancing acts is more in order. Mr Laliberté is the boss of Cirque du Soleil, a valuable global entertainment firm that has helped to transform the traditionally seedy circus business into a high-class, highly-profitable enterprise. With this growth have come management challenges galore—not least the practical difficulty of masterminding and monitoring productions around the world. Cirque currently has five different shows touring in Europe, America, Japan and New Zealand, and four permanent spectaculars in America—three of them in Las Vegas alone. This week sees the premiere of its fourth and most expensive show to date in the city—a $170m extravaganza called “Ka” at the MGM Grand hotel. In April, another touring show will debut in Montreal. Next year Cirque plans a fifth Vegas show, this time in co-operation with the surviving Beatles.

Since creating Cirque du Soleil in 1984, Mr Laliberté has developed a distinctive brand of live performance that combines traditional circus performers recruited from around the globe with opera and theatre, complete with lavish costumes, amazing sets, original music and high-tech special effects. No animals are used, as they are costly and ethically tricky. But none of this comes cheap. It requires at least $20m and more than two years to take a show from bright idea to opening night. Mr Laliberté aims to produce one new show a year, which means having three in production at a time. Revenues have grown by 15% a year since 2000, to $550m last year, thanks to the 7m people who paid up to $150 a ticket to see the latest greatest show on earth.

The 45-year-old Mr Laliberté's official title is founder and chief executive officer, but he prefers to call himself Cirque's “guide”. (Many of Cirque's staff regard him as a sort of guru.) It is he who decides on Cirque's next show, chooses its directors, and supplies the cash to allow imaginations to soar—as well as vetting and often shaping the final product (although he prefers to leave the daily running of the business to others). Like many gurus, Mr Laliberté can be elusive and baffling. “What can I say, he's an artist,” sighs Cirque's press director after yet another meeting with him is suddenly cancelled. Such antics are amusing in clowns, but alarming in the head of a firm with 3,500 employees counting on him for their bread, as well as circuses.

So far, Mr Laliberté's creative vision and commercial success have won him the confidence both of his workers and of hard-headed business partners such as MGM Mirage, which has invested hundreds of millions of dollars in building theatres for its performances. But, just in case, Cirque has started to think about the issue of succession, pinpointing young people within the company who could carry on its artistic and business tradition.

Cirque has already branched out into TV, film, music recording and merchandise. Its growth plans include further tours in Asia and permanent shows in New York, Tokyo and London. The brand is evolving, to keep both creators and audiences interested. “Ka” has taken the bold step of introducing a storyline. “Zumanity”, Cirque's Las Vegas “sex show”, has taken the company into riskier territory. Past talk of opening Cirque du Soleil hotels, with trapezes in reception and jugglers providing room service, has gone quiet, but a recent deal with Celebrity cruises to provide themed entertainment for bars has led Mr Laliberté to consider adding similar artistic value to restaurants, nightclubs and resorts. Such expansion is likely to be costly, and yet Mr Laliberté, who owns 95% of the firm, has no plans to take Cirque public. “If we lose our craziness, we will be in trouble,” says Daniel Lamarre, the firm's chief operating officer.

Cirque allocates 1% of its gross revenue to social projects— $65m so far. Much of this is spent on Cirque du Monde—circus workshops for street children in 18 countries, ranging from Brazil to Mongolia. While Cirque du Soleil has yet to recruit any of its performers directly from Cirque du Monde, there is a clear business rationale for its social programmes. A travelling circus needs to be on good terms with its neighbours, not least to minimise trouble with planning permits and local workers—from his early days organising performances in rural Quebec, Mr Laliberté learned the importance of friendly relations with his hosts. Cirque has also followed this rule at home, building its headquarters and worldwide training centre in a rundown area of Montreal, beside a massive rubbish dump. The neighbourhood has become circus city, with Canada's national circus academy pitching its tent nearby.

It takes a big top

Cirque du Soleil's social activism also helps with recruitment, appealing to the idealism of the sort of circus folk it likes to hire. Indeed, the secret to Cirque's success, says Tom DeLong, a professor at Harvard Business School, is its focus on staff, not on the audience—a striking creed at a time when most firms stress that the customer is king. Cirque even offers opportunities for career progression: young performers who start off touring can later settle down with roles in the fixed shows in Las Vegas, or in less hair-raising jobs in production or administration. Even so, Cirque's employment record is not spotless: last year, it had to pay $600,000 to settle a discrimination complaint brought by an acrobat who was found by a tribunal to have been illegally fired because he was HIV-positive.

The biggest challenge for Mr Laliberté is to retain Cirque's family atmosphere and creative spark, even as the firm grows and inevitably becomes more bureaucratic. And Mr Laliberté must also grapple with the threat-cum-compliment common to many a successful innovator: staying ahead of the competition from other modern circuses and big-budget spectaculars rushing into the

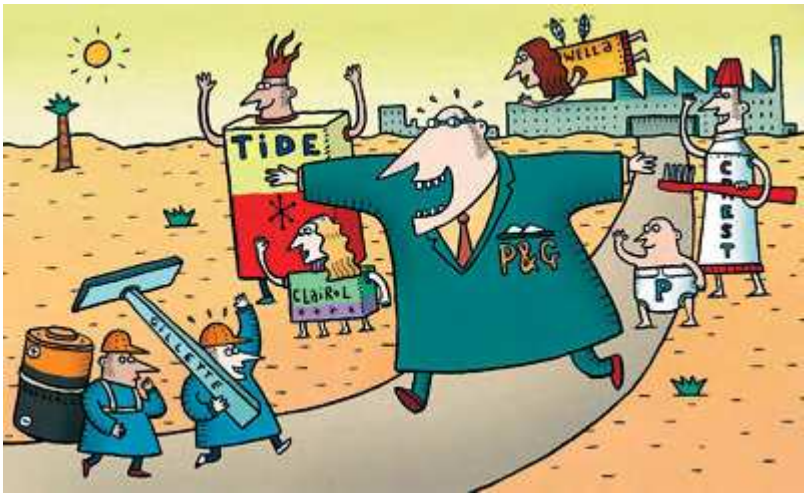
market that he created.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Consumer goods

The rise of the superbrands

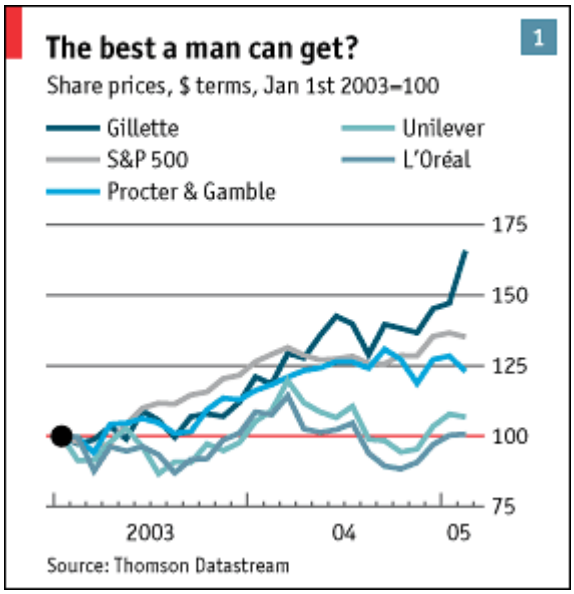
Feb 3rd 2005 | HONG KONG, NEW YORK AND PARIS
From The Economist print edition



Can Procter & Gamble's $54 billion merger with Gillette kick-start growth in the consumer-goods industry?

EVERY industry has its golden age. The makers of packaged consumer goods—quilted paper towels, tinned baked beans and other household essentials—enjoyed theirs around the middle of the 20th century. In the 1950s and 1960s, companies such as General Mills, Unilever and Procter & Gamble were delighting their customers with one innovative new product after another, from fluoride-enhanced toothpastes to fragrant fabric softeners and disposable nappies. But the industry's youthful vigour has ebbed away. Mr Clean, the bald, rugged sailor who fronts a line of domestic-cleaning products for P&G, turns 47 this year. (The chap has had a rejuvenating name change, however: he used to be called Mr Veritably Clean.)

One consumer-goods company that has fought as heroically as any against the onset of middle-age lethargy is P&G. In the past five years, the firm that was founded in Cincinnati in 1837 by William Procter, an English candlemaker and James Gamble, an Irish soap manufacturer, has boosted innovation, ditched losing brands, bought winning ones and stripped away some of the bureaucracy that has slowed its starch-shirted army of 110,000 “Proctoids”.



As P&G's share price has recaptured a little of its bounce (see chart 1), Alan (“A.G.”) Lafley, a dapper beauty-products specialist who became boss in June 2000, has grown bolder. On January 28th, he announced his company was buying Gillette—a maker of razors, shaving foam and other grooming products, as well as batteries and toothbrushes—for just over $50 billion. Stockmarket analysts and industry gurus whooped with delight. Mr Lafley called the deal a “unique opportunity” and a “terrific fit”. Gillette's boss, James Kilts (who will become a vice-chairman of the combined firm, and who stands to net more than $150m from the deal) said the merger would create “the potential for superior sustained growth”.

Even more fulsome in his praise was Warren Buffett, whose investment company, Berkshire Hathaway, owns nearly 10% of Gillette's shares. This “dream deal” would create “the greatest consumer-products company in the world”, he chortled, promising to invest more in the new firm.

The combined company will certainly be the biggest in its industry: it will have annual sales of more than $60 billion and a workforce that will top 140,000. But will it also be the best? Has Mr Lafley discovered among his shampoos, face creams and hair dyes an elixir of youth?

As Barbara Hulit of the Boston Consulting Group points out, the consumer-goods industry has found itself caught between slowing sales, rising costs and waning pricing power. Over the past five years, calculates Ms Hulit, the sales of the consumer-goods companies included in the S&P 500 index of big American companies have grown at a compound annual rate of just 4.7%. Meanwhile, their sales, general and administrative expenses have been rising by 5% a year.

Even with careful stewardship, the sales of mature brands tend to slip back towards their “natural” growth rate—population growth, plus inflation. P&G pioneered fabric softeners in the 1960s and scented sheets for tumble dryers in the 1970s. The industry introduced detergents as long ago as the 1930s. King Gillette founded the American Safety Razor Company in Boston in 1901. Ivory, a P&G-branded soap, traces its serendipitous history back to 1879, when James Gamble, son of the founder and a trained chemist, accidentally cooked up an unusually pure, floating soap in his laboratory.

Commodity prices have risen sharply recently, pushing up the cost of the foodstuffs, chemicals, packaging and energy that go into making the industry's products. There was a time when consumer-goods firms could pass rising costs on to their customers. But the spread of aggressive, big-box retail chains such as Wal-Mart (whose strategy is built around passing on savings won

from suppliers to its shoppers), Carrefour and Costco has destroyed much of the industry's pricing power.

Meanwhile, retailers have begun plugging their own discounted, “private label” brands that compete with the pricier, higher-margin products from Unilever and P&G. As retailers have grown in clout, they have also squeezed the consumer-goods firms for more “trade spending”—the money the likes of P&G must stump up for in-store promotion, displays and eye-level shelf space. About 17% of the consumer-goods industry's sales disappear into such trade spending, says Ms Hulit.

Meanwhile, the complexity of advertising, marketing and distributing branded consumer goods has soared, further pushing up costs. P&G is the world's biggest advertiser, with a budget of around $3 billion last year. A decade ago, 90% of its global advertising spending went on television. Today, for some products only about a quarter of the budget is spent on television. The audience for traditional media is fragmenting, making consumers harder and more expensive to reach. So, along with other consumer-goods companies, P&G is finding that so-called “below-the-line” forms of marketing, such as in-store promotions, posters, coupons and sponsorship, are often more effective.

Hair today

The purchase of Gillette follows two other big acquisitions since Mr Lafley took the top job at P&G. In November 2001 he bought Clairol, a hair-dye company, for $5 billion. Two years later, he spent $6.9 billion on Wella, a German beauty firm. Less noticed, but perhaps more important to P&G's rejuvenation, has been Mr Lafley's willingness to jettison tired brands.

As David Harding of Bain, a consultancy, points out, consumer-goods firms find it hard to boost growth by letting go of older, slower-growing brands. These brands have become so established in the minds of shoppers that they sell themselves, points out Mr Harding—customers buy them without thinking. That makes them a good source of profits. But they also eat up scarce management time and marketing talent on lines of business that are unlikely ever to grow much. At P&G, Mr Lafley has shed Punica, a German juice brand and Sunny Delight, an American one, Jif (peanut butter) and Crisco (pastry shortening). He has also got rid of P&G's BIZ, Milton, Sanso, Rei and Oxydol detergent brands. (The Oxydol sale must have especially hurt sentimental Proctoids: the soap powder was the proud sponsor in 1933 of “Ma Perkins”, one of America's first soap operas.)

The combined effect of these sales and purchases has been two-fold. First, Mr Lafley has given P&G's portfolio of brands a sharper focus on beauty and grooming products, where he spots more potential for growth. Second, by reinvesting cash from P&G's sales back into its strongest brands, Mr Lafley has bet more of the firm's resources on a smaller number of top “superbrands”, which are contributing more and more to the company's overall sales. In 2000, P&G owned ten brands each with annual sales of more than $1 billion. By 2004, it had 16 brands with sales over $1 billion. Together these earned the firm $30 billion of its $51.4 billion of sales that year. The purchase of Gillette, where Mr Kilts has followed a similar strategy, adds a further five superbrands. “P&G has done really well consolidating its brands down to a strong core,” says Uta Werner of Marakon Associates, a consultancy.

P&G is hoping that this growing stable of superbrands will help it to weather the industry's tough environment. Competition for the modern consumer's attention is ferocious. Steven Fredericks, the chief executive of TNS Media Intelligence, says that he adds an astonishing 400-700 new brands every day to the 2.1m brands that his New York company already tracks. These can range from a new face cream to a new model of car, or a film (which is now considered a brand).

Advertising executives in Japan reckon the number of new beverages that enter the market each year runs into the thousands. Most perish almost instantly in the relentless battle for scarce shelf-space in Japan's small shops.

The superbrands should also help P&G to focus research and development spending on the most promising products. Like Gillette, P&G prides itself on its skill in adding incremental innovations to seemingly mature products, and then persuading customers to part with more money for them. Over the years, King Gillette's safety razor has added more blades, a lubricating strip, a high-tech handle and (triumphantly, last year) an exorbitantly-priced battery-powered version featuring "micro-pulse technology".

P&G, meanwhile, has turned the humble floor mop into a "swiffer", an "all-in-one, ready-to-use mopping system" that features an "action sprayer", "premixed cleaning solution" and super-absorbent, triple-layer cleaning pads. Together, the two firms hope to transform yet more mundane household goods into technology-rich marvels. Since research suggests that the average supermarket shopper spends just a few seconds pondering each purchase and is unlikely to know the price of most items, P&G's and Gillette's push towards the frontiers of household-goods technology could prove profitable.

Merger of unequals 2

Company comparison, $bn

	Procter & Gamble*	Gillette
Sales	51.4	10.3†
Profits	6.5	2.3†
Dividends	2.5	0.7‡
R&D spending	1.8	0.2‡
Leading brands	Tide, Always, Iams, Pantene, Charmin, Bounty, Actonel, Crest, Ariel, Downy, Pampers, Pringles, Folgers, Wella, Olay, Head & Shoulders	Mach3, Gillette, Oral-B, Duracell, Braun
Employees	*110,000*	*30,000*

Source: Procter & Gamble

*Year ending June 2004 †2004 estimates ‡2003

Another trumpeted benefit of the merger is the access Gillette will win to P&G's more evolved distribution network in developing countries, where the potential growth rate for the industry's products remains higher than in America, Europe or Japan. As the world's fastest-growing big market for consumer-goods firms, China will be critical to the success of the merger. P&G's long experience there should help it to push Gillette's lesser-known brands to the mainland's rising middle classes.

Chinese lessons

P&G has the best track record of any consumer-goods firm in China, says Tom Doctoroff, the head of greater China for J. Walter Thompson, an advertising agency that is part of WPP. This is because it has bothered to learn what sells in China and, importantly, how much consumers are willing to pay for their slice of western convenience and style—still relatively little.

In shampoo, for instance, P&G's Rejoice brand has won a 25-30% share of the Chinese market. Its Olay skin-moisturising brand is a market leader and has tripled sales since 2000. The overall skin care category should double to $3.4 billion by 2010, Laurent Philippe, the head of P&G's Chinese business, said recently. But Chinese consumers are wary of new products and prefer a trusted brand. So P&G is hoping to capture its share of that growth by extending the Olay brand across a range of categories (such as whitening creams) rather than by introducing rivals.

P&G has also been quick to understand the importance of advertising on China's national television network—long considered too expensive by other multinationals. In a country where people are, from long experience, suspicious of fine-sounding claims, China Central Television (CCTV) is a much-trusted broadcaster. Unlike in the West, where media are proliferating, CCTV still dominates the airwaves, and families all across China believe in it. As a consequence, products sold on CCTV also tend to be trusted. It must feel to P&G as if it has rediscovered in China the golden age of the American mass market.

Firms such as Wahaha, which sells water, milk and soft drinks, and Haier, a white-goods group, have become household names because they have spent money advertising on CCTV. P&G was the first foreign company to take CCTV seriously. Last November, it became the biggest overall spender in the national auctions for airtime held by CCTV, paying 385m yuan ($46.5m) for advertising slots. The slots will help P&G to develop its business in central and western China and second-tier cities.

All this has translated into strong results: the group's sales in China have grown by 25% for three consecutive years, to nearly $1.8 billion at the end of 2003. Profits, meanwhile, have risen by an average of 140% a year. Already, that growth has elevated China to P&G's sixth-biggest market in 2003. It could eventually claim second place behind America.

Old Europe

In Europe, the merger of P&G and Gillette could trigger a series of takeovers or brand sales among rivals. Europe's consumer-goods firms are already struggling with the strength of the euro and rising commodity prices. As in America, there is also increasing competition from supermarkets' own brands, which are taking more shelf space. Suddenly, the two biggest European players, Unilever and L'Oréal, are looking less like giants.

Unilever, an Anglo-Dutch company, is Europe's biggest producer of consumer goods. It has been struggling to get into better shape for several years. In February 2000 it announced its “Path to Growth”, an efficiency drive that has saved about €4 billion ($5.2 billion) in costs. It also reduced its portfolio of brands from 1,600 to around 400. But it has failed to meet targets for sales and profits. The company's sales declined by 3.8% and its net profits were down 16% last year, according to estimates by Merrill Lynch, an investment bank. Last September, the company issued its first-ever profit warning. It will unveil its latest strategy on February 10th.

Some of Unilever's brands are known around the world. They range from Dove skin products to Surf washing powder to Hellmann's mayonnaise—the world's top-seller. It is also a leader in personal care. Unilever's Axe range of deodorants (sold as Lynx in Britain, Ireland and Australia) is reckoned to be the world's most popular grooming product. It was launched in America only in 2003.

P&G is already Unilever's biggest rival in health and personal care, which represents almost half of Unilever's business. Gillette competes with Unilever as a producer of toothpaste, deodorant and cologne. As a combined force, they stand a better chance of attacking Unilever's

With the addition of Gillette, P&G will almost be on

strengths. Emerging and developing markets, such as India where Unilever has a strong, local operation called Hindustan Lever, have traditionally been the company's forte. But P&G has been catching up. With the addition of Gillette, it will almost be on a par with Unilever in many areas outside Europe and America.

a par with Unilever in many areas outside Europe and America

Brazil could be an early test of the contest to come. Unilever controls a quarter of the Brazilian market for toothpaste, and P&G's product is hardly known. But Gillette has about a third of the market for toothbrushes. The merged firm can combine its effort, perhaps to launch a joint brand of toothpaste in the Brazilian market, says Lauren Lieberman, an analyst at CSFB, an investment bank.

For L'Oréal, which was founded in 1907 by a French chemist who invented a new way to colour hair, the merger could be good news—at least while P&G is distracted by making the deal work. L'Oréal has faced fierce pressure from P&G in its core hair-care market.

History suggests that rivals will try to adjust to the new competitive landscape, perhaps quickly. Unilever's acquisition of Bestfoods in 2000 triggered a wave of consolidation. Kraft, an American food company, bought Nabisco, the maker of Oreo cookies and Ritz crackers, and Pepsi bought Quaker Oats. In 2001, Nestlé paid $10.3 billion for Ralston Purina, an American pet-food company.

Even before the latest merger there was plenty of gossip about possible deals. Reckitt Benckiser, a British household-products company, was recently courted by Colgate-Palmolive, an American maker of toothpaste. P&G has also been seen as a potential buyer of Beiersdorf, a German skin-care company, and Henkel, a German maker of laundry detergent. Henkel says it does not feel especially threatened by the P&G merger as its products barely overlap with those of Gillette. Beiersdorf, on the other hand, sells lots of men's grooming products similar to those made by Gillette. But it insists it can do well on its own.

Scale or strength?

Others may now be interested in buying these companies. But Sylvain Massot, an analyst at Morgan Stanley, an investment bank, says European consumer-goods groups will first have to decide whether size is really so important. The jury is still out on whether firms focused on a few core brands will inevitably lose out to cross-category giants. Advocates of size think that a big company can leverage scale to cut costs, use these savings to invest more in advertising and innovation, and so gain even more scale.

But there are also diseconomies of scale. Giant firms can find it more difficult to move quickly, and their costs can balloon. In particular, mergers take discouragingly long to complete. P&G is still far from finished integrating Wella, for example, and may need many months, if not years, to do the same with Gillette. In any case, strong brands are more important than scale, argues Klaus-Peter Nebel, a spokesman for Beiersdorf, a company less than one-tenth the size of the new P&G. (Beiersdorf's skin cream, Nivea, is one of the strongest brands in the industry.)

Indeed, some of the most successful consumer-goods companies over the past decade have tried to become leaders in just a few product categories, relying on focus rather than scale. Reckitt Benckiser, for instance, is thriving with a limited product range. L'Oréal sold its pharmaceutical business to focus on hair and skin care. In the food industry Danone is selling only water, biscuits and yogurt, but is a world leader in all three.

Mr Lafley's latest deal is aimed at capturing the benefits of both scale and focus, creating a

business that is both larger and more reliant on a smaller portfolio of stronger brands. Barring objections from American or European competition authorities, P&G's acquisition of Gillette should achieve this. Whether the new merged firm will then be able to rekindle the consumer-goods industry's dreams of youth remains to be seen.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

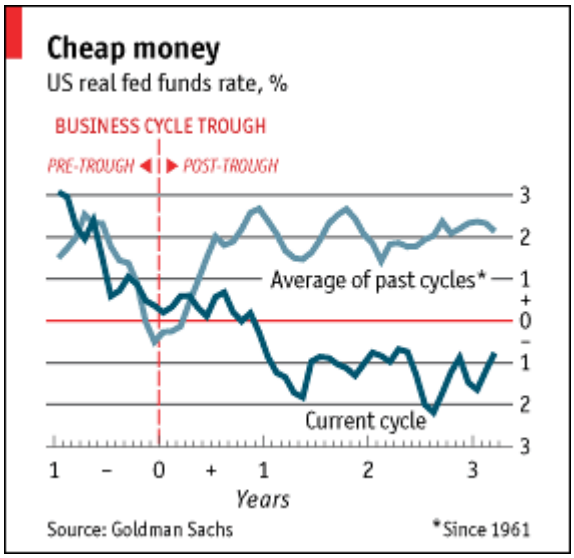
The world economy

Still gushing forth

Feb 3rd 2005
From The Economist print edition

The global economy is awash with liquidity, pumped by America

THIS week, as widely expected, Alan Greenspan and his colleagues at America's Federal Reserve raised the federal funds rate for the sixth time since last June, to 2.5%. Six rate rises at six successive meetings may sound tough, yet real interest rates (estimated by the federal funds rate less the headline rate of consumer-price inflation) are still negative. And not content with running a lax monetary policy at home, America is also exporting its super-loose ways around the globe.



America's monetary policy is still extraordinarily slack. Real interest rates are three percentage points lower than they have been, on average, at the same stage of previous economic recoveries since 1961 (see chart). Furthermore, according to an index compiled by Goldman Sachs, overall monetary conditions are still slightly easier today than when the Fed started tightening last June: a weaker dollar, lower bond yields and higher share prices have offset higher short-term interest rates. Even so, futures contracts suggest that the financial markets expect interest rates to be raised to only 3.5% by the end of 2005, leaving real rates still quite low.

Considering how loose policy is, inflation remains tame. America's headline inflation rate was 3.3% in December; the core rate (excluding food and energy) was 2.2%. However, there are plenty of other signs that easy money has led to excess, from rapid growth in credit and house prices to tight credit spreads and a widespread willingness to take greater risk. The minutes of the Fed's monetary-policy meeting in December suggested that some central-bank officials have started to worry that speculation is getting out of hand in some quarters, notably the housing market. If this carries on, the Fed may raise rates by more this year than the markets expect.

The weaker dollar, which has helped to keep overall financial conditions loose in America, will be on the agenda when finance ministers and central-bank governors of the G7 countries meet in London on February 4th and 5th. Although the dollar has rallied this year, it is still 6% weaker against the euro than when the G7 last met in October and worth 35% less than in early 2002. Yet, despite the dollar's slide, America's trade deficit continues to widen. China, which has been invited to the G7 meeting, is likely to be cast as the villain and to come under renewed pressure to revalue its currency. The Chinese are likely to turn a deaf ear.

When the G7 last met, ministers and officials celebrated the fact that the world economy was growing at an annual rate of 5%, its fastest for almost 30 years. It has since slowed, mainly because of weaker growth in America and Japan. In the fourth quarter of last year, America's GDP growth fell to 3.1% at an annual rate, from 4% in the previous quarter. But the slowdown was largely due to the widening trade deficit; consumer spending surged at an annual rate of 4.6%.

The only real remedy for America's huge external deficit is a tightening of its monetary and fiscal policies to boost domestic saving. Many Americans favour a weaker dollar as a less painful way to trim the deficit. However, a fall in the dollar alone will not make much of a dent in the trade gap. America also needs to cut its budget deficit and to raise interest rates to curb consumer spending. That could necessitate a marked slowing of economic growth. America's policymakers prefer not to contemplate this.

The global gusher

It is not just America that feels the effect of low American interest rates. America has flooded the whole world with liquidity. Its loose monetary policy has been exported to other central banks through the fall in the dollar. For example, to offset the impact of a stronger euro on growth, the European Central Bank has been forced to hold the euro area's real interest rates negative for longer than might otherwise have been prudent. Mortgage lending in the single-currency zone is rising at an annual rate of 10%. In many countries, notably France and Spain, house prices are booming.

America's easy money has also spilled beyond its borders in a second way. When central banks buy American Treasury bonds, adding to their foreign-exchange reserves, to try to hold down their currencies against the dollar, they print local money. This amplifies the Fed's lax stance. Last year, the global supply of dollars (the sum of America's monetary base plus global foreign-exchange reserves) rose by a whopping 25%. After adjusting for inflation, this is close to the fastest pace in the past three decades.

Worse still, the effects of greater global liquidity then flow back into America's economy. By buying huge amounts of American securities to prevent their currencies rising, Asian central banks depress American bond yields, lowering borrowing costs for home buyers and companies. By some estimates, Asian purchases of American bonds have reduced yields by between half and one percentage-point.

The flood of global liquidity has not, as in the past, pushed up inflation in the prices of goods and services. Instead it has inflated a series of asset-price bubbles and encouraged investors to take ever greater risks. Several structural factors, such as the IT revolution, deregulation and competition from cheaper Chinese goods, have helped to hold down traditional inflation—and hence interest rates—in rich economies. The increased credibility of central banks also means that they need to raise interest rates by less than in the past to choke off inflationary pressures.

Yet many of those very same structural forces that help to hold down inflation and interest rates, such as the entry of China into the world economy, have also increased the global return on capital and so lifted the real neutral rate of interest for which central banks need to aim—ie, the rate that neither stimulates nor reins in the economy. Inflation stays modest, but holding interest rates too low for too long creates excess liquidity, which is now more likely to spill into the prices of homes, shares or other assets than those of goods and services.

Measured by the growth in global credit or property prices, the world economy is experiencing a severe episode of inflation. Inflation has simply taken a different form. The Fed insists that it is not its job to respond to rising asset prices. But the risk is not just that asset-price and credit bubbles eventually burst but, as with traditional inflation, that surging asset prices distort relative prices and cause a misallocation of resources. For instance, because households think they are wealthier, they spend more and save and invest less. The cost is lower living standards tomorrow.

The source of the current problem is that, although the Fed refuses to constrain asset prices, it reacted to the bursting of the stockmarket bubble by pumping out yet more liquidity. The risk is that as interest rates rise the fragility of the economic recovery will be revealed. Decisions based on cheap credit will look less than wise.

Mr Greenspan, the Fed's chairman, now has less than one year left in his job. His term ends on January 31st 2006. His successor may need to think harder about the fact that the Fed is, in effect, the world's central bank, and thus about the global ramifications of its policies. He or she may at some stage also have to contend with a painful economic hangover. Does anybody really

want the job?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The G7 finance ministers' meeting

Africa expects

Feb 3rd 2005 | JOHANNESBURG
From The Economist print edition

Hoping for actions, not just words

WHEN Nelson Mandela asks a favour, it is hard to refuse. So pay attention this weekend when the G7 finance ministers meet in London to see whom Madiba, as South Africa's ex-president is fondly known, sweet-talks. Invited by Britain's Gordon Brown, he has a specific role to play. The heads of government summit in July is supposed to focus on Africa. And Mr Mandela will be able to bring moral pressure to bear on anyone steeled against Britain's plans for more aid, debt relief and trade concessions for the continent. Watch to see whether Madiba's arm goes around the shoulders of the penny-pinching German or American representatives.

Africa's hopes are high. A group of leaders, notably Thabo Mbeki, South Africa's current president, has long pushed a simple proposal: if Africans govern themselves better, as they appear to be doing (wars seem to be declining; some rulers are proving honest and democratic), rich countries should invest more and give more aid. The rich have promised to give a total of only 0.7% of their GDP in foreign aid; in fact, they give far less than that.

Of course, grand schemes to help Africa have failed dismally in the past. Cynics say that the latest is a ruse by the British government, embodied in its Commission for Africa, to show a soft face in foreign policy ahead of a general election. So Africans want long-term commitments: for example, governments and businessmen have earmarked 20 infrastructure projects around the continent, in energy, transport and irrigation, that would boost private economic activity. Donors might make specific pledges to finance these.

African finance ministers who met in Cape Town last month suggested that parts of the continent could usefully absorb much more aid than they get. They like Mr Brown's idea for an International Finance Facility, to lend to Africa against promises of future aid from rich countries. The challenge, though, is to spend any extra money well. That means focusing on better-run countries.

Which, though? One way of choosing is to use the results of the African Peer Review Mechanism, under which governments are visited by experts from elsewhere in Africa who offer advice on how to run countries better. That is likely to produce the usual list (Ghana, Senegal and some others): basket cases like Zimbabwe will not even get a mention.

The Africans would like to see progress on trade too. They believe, with some cause, that the Doha round of world trade talks has lost momentum, with rich countries unwilling to slash farm subsidies and other barriers that limit trade with poor ones. Bright ideas are also needed on how to boost African capacity to trade, by fixing up harbours or sending technical expertise to help with trade negotiations.

Then there is debt. Britain favours large-scale relief: a figure of $80 billion is being thrown around. Not everyone thinks this a good idea: those with a decent credit rating, such as Botswana, might

worry that a write-off could put investors off the whole continent. But big aid spenders, such as Japan, may prefer cancelling debt to paying for tricky projects in remote bits of Africa. It should be a busy weekend.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Citigroup and MetLife

Out of life

Feb 3rd 2005 | NEW YORK
From The Economist print edition

America's biggest bank completes its exit from insurance

MORE than six years on, the reasons for Citicorp's merger with Travelers, a big insurer, in October 1998 remain sound. Moody's, a rating agency, says the value of diversification alone has played a role in boosting the credit rating of the giant now known as Citigroup. With its enormous distribution network of branches and Smith Barney brokers, as well as a missionary salesforce of more than 100,000 part-timers, Citigroup was well equipped to push insurance policies—products that, as industry lore has it, are sold not bought.

Nevertheless, on January 31st Citigroup said that it was selling its life and annuities division to MetLife, America's second-biggest life insurer, for $11.5 billion. The price is hardly dear. MetLife is paying less than 13 times last year's earnings for a vast book of business and access to Citigroup's huge distribution network. Citigroup clearly wants to be rid of insurance. Having spun off Travelers' property and casualty arm in 2002, it has largely dumped a business that not long ago it sought to expand.

Citigroup says that insurance has worse growth prospects and a lower return on capital than its other businesses. Fine—but that argument implies that it should concentrate on credit cards, Smith Barney and consumer finance, and quit everything else, including retail banking. The question is why Citigroup should frown on insurance in particular. It might point to MetLife's own return on equity of only 11%, compared with Citigroup's 19%. But MetLife's low number is partly an illusion. Its earnings have grown by 22% a year since it announced its demutualisation in 1999, faster than Citigroup's more than decent 14%, according to Value Line, a stock-analysis firm. Its book value has grown dramatically, holding down its return on equity. The financing of this week's purchase should by itself improve the figure.

Both Citigroup and MetLife pointed to the consolidation of America's insurance industry as a justification for the deal. Mergers are indeed taking place: last spring, Manulife Financial bought John Hancock for $10 billion, and MetLife has made a number of tiny deals. However, scale is no guarantee of success. A study of 79 insurance companies by SNL Financial, a research firm, concludes that there is no correlation between size and returns.

After the deal, several commentators remarked that it amounted to an admission by Citigroup that banks may be ill-suited to selling insurance. Whether they are or not is hard to say. The evidence from America is shaky because until Citicorp and Travelers came together, joint ownership had not been generally permitted for 60 years. An exception existed for Wells Fargo, a San Francisco bank, which is apparently succeeding. Citigroup itself has a Mexican operation, Banamex, that has done so well selling banking and insurance that it was excluded from the MetLife deal. In Europe, where the combination is more common than in America, there have been both successes and failures.

Indeed, Citigroup has not done at all badly out of insurance, despite its own glum assessment. In

the fourth quarter, insurance provided a better return than the group's huge capital-markets businesses, which are certainly not for sale. Citigroup did have trouble selling property and casualty insurance: an effort to push auto policies on to credit-card holders failed. But it quit that business in 2002. Life insurance should have been an easier fit, being more closely related to the investment products sold by the company's brokers.

So why should Citigroup sell? Possibly, it is trying to steer clear of potential conflicts of interest, or the appearance of them. In the past three years the firm has undergone one investigation after another stemming from its mishandling of conflicts between its own interests and those of its clients—most obviously, in its investment bank. In insurance, there is a possible problem when a financial adviser, who has a fiduciary duty to a client, is tempted to push an in-house product that would generate not only a sales fee but also a running management charge. Annuities—in essence, life policies strapped on to mutual funds—are one common example of how this might arise. Typically, the clarity of the products is poor; the fees are high. Regulators are looking into annuity sales, so any prudent firm might be worried. Similar conflicts exist when brokerage firms push proprietary mutual funds. Citigroup's asset-management operations happen to produce lower returns than insurance. It would not be a shock if they were sold too.

Charles Prince, Citigroup's chief executive, has denied that the deal was motivated by regulatory concerns and said that the asset-management unit was not for sale. It would have been hard for him to say anything else. The market, though, thinks that Citigroup has made a good deal, despite the low price it has received and its fair performance in the life business. Citigroup's shares, embattled of late, popped up; MetLife's, as those of purchasers are wont to do, went down.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Marsh & McLennan

Settled, at a price

Feb 3rd 2005
From The Economist print edition

A vast settlement between Eliot Spitzer and the giant insurance broker

HOW much does it cost to shake off Eliot Spitzer, New York's tireless attorney-general? For Marsh & McLennan, the world's largest insurance broker, the answer is $850m. On January 31st Marsh agreed to pay that sum to settle civil charges of rigging bids for insurance contracts and sending clients to favoured insurers, in a suit brought by Mr Spitzer and New York state's insurance superintendent. Marsh will pay no fines. Instead, all the money will go into a fund to compensate policyholders in several instalments, ending in 2008.

Even for a company of Marsh's size, $850m is a lot of money, although Michael Cherkasky, its chief executive, says the payments “will not threaten the company's viability”. Marsh will fork out more than any other financial-services firm targeted by Mr Spitzer. Last year's biggest haul was the $375m which Bank of America paid to settle allegations, made by the Securities and Exchange Commission as well as Mr Spitzer, of mutual-fund misconduct. Marsh's sum is almost two-thirds of what ten Wall Street firms together paid in 2003 to settle charges brought by several regulators, led by Mr Spitzer, that the firms' analysts had played up the shares that their investment-banking colleagues were hawking at the same time.

The Marsh settlement's wording is almost as eye-catching as its price tag. In common with other firms skewered by Mr Spitzer, Marsh neither admitted nor denied wrongdoing. Though coy about its own guilt, it issued a statement castigating some former employees for having “unlawfully deceived their customers” and indulging in “shameful” conduct. Marsh also released a report from an internal investigation, which found that discussions of bid-rigging “took place regularly” among certain employees.

This nice distinction between errant employees and their employer owes much to the pile of lawsuits Marsh is likely to face from shareholders, policyholders who do not opt into the settlement, and other states' insurance commissioners and attorneys-general, who have also been investigating the company. Connecticut is already bringing civil charges against Marsh and ACE, an insurer, alleging a concealed kickback between the two. Marsh hopes to head off the state regulators by compensating policyholders and by carefully dividing the New York settlement money by state (Californian clients will get $131m, Texans $55m and so on). Still, Morgan Stanley estimated before this week's settlement that legal action could cost Marsh $2 billion in all.

What next? As well as trying to keep clients and bracing itself for lawsuits, Marsh has been making changes. Mr Cherkasky, who became chief executive in mid-crisis in October, has cut jobs and disbanded the firm's “global broking” arm, the centre of the bid-rigging charges. Unlike some competitors, Marsh has also banned contingent commissions (payments insurers make to brokers in exchange for getting more business), which can make brokers more loyal to insurers than to their clients. The amount of this week's settlement just about matches the $845m Marsh received in 2003 in such fees.

The insurance industry as a whole nervously awaits more fire-breathing from Mr Spitzer. He has subpoenaed lots of companies and already wrung guilty pleas from six executives, including one at Marsh. He says more such pleas are likely. Insurers and brokers can only hope that the attorney-general will soon be distracted by his bid to be elected governor of New York in 2006. Trouble is, note some in the industry glumly, in New York the governor appoints the insurance superintendent.

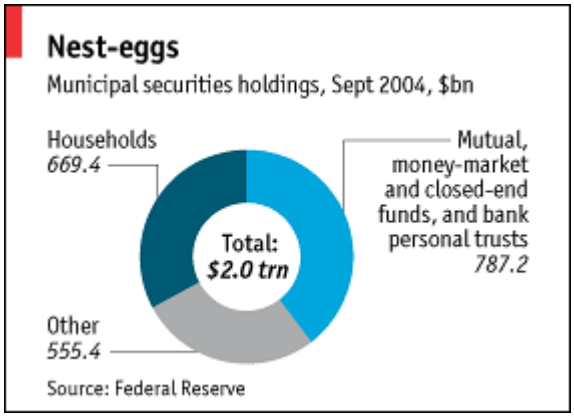
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Municipal bonds

Let there be light

Feb 3rd 2005
From The Economist print edition

Bond trading in America is getting more transparent. Not before time



WHILE most of the bond-buying world was waiting this week for America's Federal Reserve to give a steer on interest rates, in a usually snoozy corner of the market business was buzzing. On January 31st, the Bond Market Association (BMA) started to display the prices of municipal-bond trades within 15 minutes of completion. The BMA says that its website normally gets 2m-3m hits a month; on January 31st alone it got 6m-7m. Those numbers should rise on February 7th, when virtually all corporate-bond prices will also be shown in almost real time.

This shines a searchlight into a murky market that is widely seen as the last refuge of the broker-dealer. With more than $2 trillion-worth of bonds outstanding and new issues last year of $358 billion, the centuries-old, largely tax-exempt municipal-bond market plays a big role in helping state and local governments to raise money cheaply for projects as grand as the Erie Canal and as petty as golf courses in Pennsylvania.

But the lack of publicly available prices—as well as the fact that most bond dealers do not tell their customers how much they themselves are making on a trade—has meant that dealers can trade securities at exaggerated spreads between the prices at which they buy and sell them. Last summer, the National Association of Securities Dealers fined eight broker-dealers for “abusive pricing”.

Bond markets in most places are far less transparent than equity markets. The argument is that the big institutional investors that dominate them do not need the same protection as mom-and-pop investors in shares. In the muni market, however, this argument makes particularly little sense.

Individuals own about a third of all such bonds directly, and perhaps another third via pension

funds, mutual funds and the like (see chart). About 80% of trades are smallish, accounting for less than 10% of the total par value traded, points out Christopher Taylor, executive director of the Municipal Securities Rulemaking Board (MSRB), which collects and disseminates the prices. Individuals—especially rich ones—are happy to take lower yields in exchange for the tax exemption most munis enjoy. But transaction costs for retail buyers of municipal bonds are about two-thirds again as high as in corporate-bond trades and nearly six times higher than in equities, said a study by the Securities and Exchange Commission (SEC), published last September and using 2003 data.

The drive to make municipal-bond trading more transparent began more than a decade ago, supported by the SEC. Since 1995 dealers have reported their trades overnight to the MSRB, and since June 2003 the traded prices have been made available the next day. Corporate-bond prices, too, have gradually been coming into the light, beginning in 2002. From February 7th, trades in all except the most illiquid and idiosyncratic will be published within 30 minutes; from July, within 15 minutes. All investors will then be looking at the same prices at the same time.

Most believe that the availability of real-time prices will eventually narrow spreads. The SEC reckoned last year that disclosure in the corporate-bond market would reduce transaction costs there by at least $1 billion a year. Lawrence Harris, who used to be the SEC's chief economist and now teaches at the Marshall Business School at the University of Southern California, thinks that eventually retail investors may see annual savings of some $200m. The real change will come when the information is made available at the point of sale, however.

There may be inherent limits, too, to what disclosure can do. Unlike most corporate bonds, municipals tend to be wildly dissimilar. They are also sticky: only a third of the issues trade at all in any given year. So deducing a price for one illiquid bond from a plausible substitute, says Arthur Warga, dean of the Bauer College of Business at the University of Houston, is “a much more heroic exercise in municipals than it is in the corporate-bond market, to say nothing of Treasuries”.

Kevin Olson, who runs a website, MunicipalBonds.com, dedicated to winkling out the worst deals in the muni market, sees other obstacles too. He says that spreads have narrowed since next-day publication was introduced, but that they are still too wide: one prime stinker this week had a spread of almost ten percentage points. “It is not just getting the information, it is getting the information out there to investors who know what to do with it,” he says. You can turn on the light, but you can't make people see.

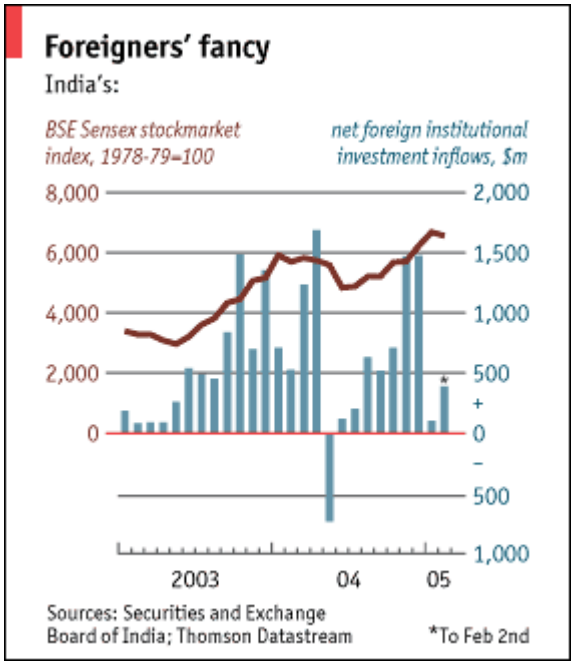
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Reforming India's equity market

Loosening up

Feb 3rd 2005
From The Economist print edition

India's government takes another step towards financial-market reform



Get article background

BIT by bit, India's financial system is undergoing overdue reform. Recently, the government relaxed the rules on foreign companies in joint-ventures with Indian partners. Changes in the regulation of bank ownership are in the works—although they seem to have been delayed by a dispute between the reform-minded finance ministry and the cautious central bank. And last week the finance ministry loosened restrictions on India's pension funds, which should in turn help the country's equity market.

The ministry says that from April non-government "provident" funds (in essence, employee pension funds) may invest 5% of their new inflows directly in shares. A further 10% can be put into equity-linked mutual funds. Provident funds manage over 1.5 trillion rupees ($34 billion) in assets—currently, all of it in government-guaranteed securities or in debt instruments issued by government-owned companies and banks. Any money received when earlier investments mature will also be subject to the new rule.

According to one observer in Mumbai, over the next 18 months perhaps a quarter of the provident funds' assets are likely to mature. In all, more than 200 billion rupees are likely to be available for

investment in the stockmarket, either directly or through mutual funds. About 100 billion rupees can be invested in the first year of the new system.

This should reduce the reliance of the Indian stockmarket on foreign institutional investors. Less than 1% of Indian household savings are invested in equity markets, and the market tends to swing as foreigners' interest waxes and wanes (see chart). Not surprisingly, the stockmarket welcomed the rule change: the Bombay Stock Exchange's Sensex index jumped 5% in two days after the announcement.

The country's mutual-fund industry should also benefit. At present, it manages just 300 billion rupees in equity assets, or 1.5% of market capitalisation. (By contrast, American funds' share of their country's stockmarket is perhaps 20%.) Many believe that provident funds, which lack fund-management skills, will prefer to place money with mutual funds rather than buy shares directly, at least at first.

However, Gautam Bharadwaj, a consultant to the Indian Ministry of Finance on pension reform, says that the new rule issued by the finance ministry has to be ratified by the labour ministry. A similar reform, allowing up to 10% of pension-fund money to be invested in shares, has been blocked by the labour ministry for the past five years, he said.

The labour ministry cannot halt the new plan altogether, but its rejection would stop the participation of the Employees' Provident Fund Organisation (EPFO), a government body that manages money for 27m of the 35m people covered by the pension schemes. The independent provident funds would then also hesitate.

Possibly to sweeten political opposition to the change, the finance ministry said on February 2nd that the minimum return provident funds must offer will rise from 8.5% to 9.5%. For EPFO-managed funds, this guarantee is the state's responsibility—so the increase may put further strain on the government's already wobbly finances. Privately managed funds have to meet the minimum from their own resources in the event of a shortfall.

This is a step back: a truly market-oriented reform would be to weaken, or even scrap, the guarantee. More reforms are planned. Expert committees have recommended privatising the asset-management function of the EPFO. They would also like to see more privately managed, individually funded defined-contribution schemes. What concessions might be needed to get these through?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Plastic money

A durable idea

Feb 3rd 2005 | NEW YORK
From The Economist print edition

The rising popularity of plastic payment, in all its forms

IN THE past few months, central bankers and currency traders have spent many hours contemplating the resilience of the dollar. To technologists at the American Treasury Department's Bureau of Engraving and Printing, this has a more literal meaning. They are testing—as they have been, off and on, for the better part of a decade—various plastic (technically, “polymer”) banknotes, comparing their qualities with those of America's traditional paper money.

Several countries have already switched from paper to plastic, at least in part. Last week, having had plastic 20-peso notes since 2002, Mexico decided to issue its 50-peso note in plastic too. In all, 23 countries, including Kuwait, Indonesia, Chile and Zambia, have issued plastic notes. Some of these countries have used polymer only for commemorative bills: these include China, where paper money was first used in the seventh century, and Brazil, where an experiment with plastic in 2000 proved unpopular. However, Australia, New Zealand and Romania have changed all their notes to plastic.

Pioneered by Australia in 1988, polymer notes have several advantages over paper ones. They are harder to counterfeit. The Mexican notes, for instance, have a clear security window that is difficult to forge. Plastic notes are also less prone to tearing, lasting four times as long as the average paper bill, and carry fewer germs, because paper absorbs sweat and moisture more easily.

However, the European Central Bank stuck to paper when issuing euro notes for the first time in 2002. America has no plans to change yet. Its officials claim that the blend of paper they use gives one-dollar bills a 21-month life, compared with 15 months for low-value polymer bills. Changing infrastructure to manufacture and to process plastic money would be pricey. And Americans might find plastic money too cheap-looking and strange.

America may not be adopting plastic cash, but it is using plastic means of payment more than ever. In December, the Federal Reserve said that electronic payments—using debit and credit cards and so forth—have exceeded cheque payments for the first time. Fuelling this have been debit-card transactions, which grew by 24% between 2000 and 2003. The use of cheques fell by 4%. The Fed, expecting this to continue, said last summer that it would close nine cheque-processing plants. With utilities, subway-token machines, highway toll booths and even McDonald's all now accepting cards, plastic is looking durable.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economics focus

The economics of sharing

Feb 3rd 2005
From The Economist print edition

Technology increases the ability of people to share, but will they share more than just technology?

BY NOW, most people who use computers have heard of the "open source" movement, even if they are not sure what it is. It is a way of making software (and increasingly, other things as well), which relies on the individual contributions of thousands of programmers. The resulting programs are owned by no one and are free for all to use. The software is copyrighted only to ensure it remains free to use and enhance. In essence, therefore, open source involves two things: putting spare capacity (geeks' surplus time and skill) into economic production; and sharing.

Economists have not always found it easy to explain why self-interested people would freely share scarce, privately owned resources. Their understanding, though, is much clearer than it was 20 or 30 years ago: co-operation, especially when repeated, can breed reciprocity and trust, to the benefit of all. In the context of open source, much has been written about why people would share technical talent, giving away something that they also sell by holding a job in the information-technology industry. The reason often seems to be that writing open-source software increases the authors' prestige among their peers or gains them experience that might help them in the job market, not to mention that they also find it fun.

The characteristics of information—be it software, text or even biotech research—make it an economically obvious thing to share. It is a "non-rival" good: ie, your use of it does not interfere with my use. Better still, there are network effects: ie, the more people who use it, the more useful it is to any individual user. Best of all, the existence of the internet means that the costs of sharing are remarkably low. The cost of distribution is negligible, and co-ordination is easy because people can easily find others with similar goals and can contribute when convenient.

The question is, can sharing be used to supply more than just information? One of the most articulate proponents of the open-source approach, Yochai Benkler of Yale Law School, argues in a recent paper* that sharing is emerging for certain physical, rivalrous goods and will probably increase due to advances in technology. Where open source was about sharing information by way of the internet, what is happening now, Mr Benkler notes, is the sharing of the tangible tools of technology themselves, like computing power and bandwidth. This is because they are widely distributed among individuals, and sold in such a way that there is inherent (and abundant) unused capacity.

Consider computing power. By some measures, the world's most powerful supercomputer is not owned by NEC or IBM, but is a volunteer project called SETI@home that aggregates the spare processing power of around 4m computers. When an individual's PC is idle, a screen-saver application that users have downloaded kicks in and harnesses the computer's processor to decode radio signals in search of extra-terrestrial life. A basic PC chip is a rivalrous good, but it

provides far more power than most computer owners ever use. So putting this spare capacity to use through sharing makes more sense, if this is as easy to do as it is with SETI@home, than letting it go to waste. Why do people not sell the capacity instead? Probably, this would raise the transaction costs to the point where it would not be worthwhile.

Moreover, via “peer-to-peer” systems, people exchange digital copies of music over the internet, sharing not only songs but, more important, the physical memory of their PCs. Tens of millions of people have used peer-to-peer systems, which account for more than half of all internet traffic. One reason why sharing is so commonplace is that there is enormous overcapacity in both computer memory and internet bandwidth (and because the songs themselves are “non-rivalrous”). Both memory and bandwidth are rivalrous, yet people have no choice but to buy more than they can usually consume themselves. And as with open source, sharing is made easy because the internet has made transaction costs so low.

Tune in and share

The phenomenon of sharing physical goods has important implications for a number of public policy debates today, most notably for regulation of the use of radio spectrum. Around the world, regulators have granted licences, giving mobile-phone companies the rights to use a specific band of the airwaves, often in exchange for billions of dollars. Spectrum is parcelled out in this way under the assumption that more than one signal on the same frequency results in interference. This has been true until recently, but today radios with cheap microprocessors can pick out competing signals intelligently, just as the human ear can make sense of a conversation in a noisy bar.

The result is that new technology has made the sharing of spectrum possible—radio waves could be a non-rivalrous good—if only this were legally permitted and engineered into the software that runs the wireless devices. Regulators have changed their approaches slightly by allowing secondary markets in spectrum, but this anachronistically still presumes exclusive, not shared, use.

Mr Benkler does not limit his analysis to computing and bandwidth, but tries to make a broader point in favour of sharing goods far beyond information technology. “Social sharing”, he asserts, represents “a third mode of organising economic production, alongside markets and the state.” However, with the exception of carpooling, he acknowledges he is hard-pressed to find instances where sustained sharing of valuable things is prevalent in the world outside information technology. For most goods and services, sharing will remain the exception not the rule. But Mr Benkler has identified an intriguing alternative.

---

* “Sharing Nicely: On Shareable Goods and the Emergence of Sharing as a Modality of Economic Production.” *Yale Law Journal*, November 2004

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Climate change and politics

Hotting up

Feb 3rd 2005
From The Economist print edition

Getty Images

The debate over global warming is getting rancorous

Get article background

“THE intermixing of science and politics is a bad combination, with a bad history.” So warns Michael Crichton at the end of his current, popular novel, “State of Fear”. He argues that wilful obfuscation by politicians and wild-eyed greens is leading to a herd mentality over global warming, akin to the uncritical embrace of eugenics a century ago. “Once again,” he intones ominously, “critics are few and harshly dealt with.”

At first blush, it appears that Dr Crichton might have a point. Of course, there was once an intense global debate over global warming's most sacred cow—the Kyoto protocol on climate change. The treaty calls for immediate reductions in emissions of greenhouse gases by industrialised countries. George Bush upset many greens by abruptly confirming in 2001 that America would never ratify the Kyoto treaty. But other countries did ratify it, and it is due to come into full force for them on February 16th, so the Kyoto debate is over.

The concern about crusading politicians also seems relevant. Tony Blair, Britain's prime minister, says climate change is his top priority, along with Africa, this year. He asked Sir David King, his chief science adviser, to organise a scientific conference in Britain this week to work out what adds up to “dangerous interference” with the climate system. The conference had not ended as *The Economist* went to press, but there was talk of pressure from politicians for agreement on a specific numerical definition of what is “dangerous”—a notion some participants said was not

justified by the science.

They said, they said

Despite Kyoto's coming into force, vigorous debate between and among climate sceptics and climate hawks continues. First, consider the ongoing haggling over the science. The Intergovernmental Panel on Climate Change (IPCC), a body of leading scientists which advises the UN on climate issues, has established that the Earth is indeed warming, thanks in part to man's burning of fossil fuels. However, questions still remain as to the particulars.

For example, when Kevin Trenberth, head of the IPCC's panel on hurricanes, recently suggested that there exists a link between climate change and the wave of powerful hurricanes last year, he was immediately challenged. Christopher Landsea, a hurricane expert at America's National Oceanic and Atmospheric Administration, resigned from the IPCC panel, arguing that Dr Trenberth's comments went beyond what the peer-reviewed science could justify. He wrote a public letter complaining that: “because of Dr Trenberth's pronouncements, the IPCC process has been subverted and compromised, its neutrality lost.”

Dr Trenberth retorts that “politics is very strong in what is going on, but it is all coming from Landsea and colleagues. He is linked to the sceptics.” He explains the remarks in question by saying that he did not suggest climate change was affecting the number of hurricanes, but was affecting their intensity, because of hotter ocean temperatures, a conclusion he says the data readily bears out.

Another example is the controversy over the most important totem of global warming: the “hockey stick”. That is the nickname given to the plot of global temperatures published by Michael Mann, then of the University of Massachusetts in Amherst, and his colleagues in 1998, which shows a sharp upturn beginning at the time of the industrial revolution. This chart has often been trotted out as the clinching proof of anthropogenic warming. Sceptics have never liked this chart, which necessarily relies on statistics to infer historical temperatures from tree rings.

Two critics, Stephen McIntyre of the Northwest Exploration Company, in Toronto, and Ross McKitrick of the University of Guelph, also in Ontario, are about to publish a paper in *Geophysical Research Letters* (GRL), which alleges that Dr Mann's statistics are inaccurate, and that the hockey stick is a mere statistical artefact. Dr Mann and many other climate scientists dismiss Mr McIntrye's and Dr McKitrick's arguments.

The statistical issues involved are complicated—even Stephen Mackwell, the editor-in-chief of GRL, which also published some of Dr Mann's earlier papers (along with *Nature*), admits that he does not understand the details of the new paper.

The debate over the economics of warming is, if such a thing were possible, even more robust than the one over the science. The IPCC has come under attack for its scenarios of future growth. One chief sin is the reliance by IPCC modellers on market-based exchange rates instead of purchasing-power parity, which adjust wealth according to domestic purchasing power—which many economists believe is more accurate. That, says David Henderson, an economist at London's Westminster Business School, leads to unrealistic projections for economic growth and therefore emissions growth. He and Ian Castles provided the IPCC with detailed critiques.

Did the IPCC welcome the chance to improve its projections? Initially, it most certainly did not. Dr Henderson was frustrated by that reaction. However, he was encouraged to learn this week that serious economists were cloistered away at a recent meeting studying ways of incorporating his critiques into the IPCC modelling process. Whether any substantive changes will emerge remains

unclear, but a proper re-think may be in the works.

Disagreements are also breaking out among those economists relatively sceptical about the effects of climate change. The Copenhagen Consensus, a project led by Bjorn Lomborg, a professor at the University of Aarhus, in Denmark, and publicised by this newspaper, made something of a splash a few months ago by ranking climate change at the bottom of a list of pressing global problems (see articles). A panel of eminent economists, among them three Nobel prize-winners, placed initiatives to tackle HIV/AIDS, malaria, sanitation and other problems confronting the world's poor ahead of proposals to tackle global warming, which were described as “bad” investments compared with those aimed at tackling these other problems. But several participants now say that there was confusion about how they were ranking ways to spend development aid, or ranking which general global problems should be tackled.

Of course, greens howled in protest at the dismissal of climate change, and pointed to some sort of stitch up: after all, some argued, Dr Lomborg is well known for his opposition to the Kyoto treaty. He rejects such claims, insisting that the effort was in good faith. He points out that the man selected to write the “expert paper” on climate, William Cline of the Centre for Global Development, a think-tank based in Washington, DC, has impeccable credentials; indeed, he is known as an advocate of forceful, early action to slow global warming. Dr Lomborg explains that the proposals on climate change fared poorly because they offered the lowest benefits for the costs incurred.

Now, some members of the Consensus are dissenting. Thomas Schelling of the University of Maryland, who voted on the final choices, thinks that presenting climate change at the bottom of the list as “bad” is misleading. He says he and the other gurus did not like Kyoto or the aggressive proposals made by Dr Cline, whom he sees as the “most alarmist of the serious climate policy experts”, but Dr Schelling says he would have ranked modest climate proposals higher on the list, because he sees climate as a real problem. Robert Mendelsohn, a conservative Yale economist who was an official “critic” of the climate paper in this process, goes further: because Dr Cline's positions are “well out of the mainstream”, he had no choice but to reject them. He worries that “climate change was set up to fail.”

Dr Lomborg insists that that was not at all the case. Picking an enthusiast like Dr Cline also could suggest that climate was being taken seriously by the Copenhagen process. However, he accepts that more modest proposals (such as a small carbon tax or investments in research) would have ranked higher on the list. Dr Cline, for his part, acknowledges that his views (for example, on the right discount rates to use when pondering long-term policies) “have not yet been accepted by the mainstream.” He is unhappy with how climate has been portrayed by the Copenhagen process, but he still feels that the attempt to assess global problems was well intentioned and worthwhile.

The death of environmentalism?

Perhaps the clearest sign that the imminent arrival into force of Kyoto has not led to a bout of green triumphalism comes from the debate among America's greens today. Michael Shellenberger and Ted Nordhaus, political strategists and green organisers, argue in a recent policy paper that, judging from polling data, America's big environmental groups have failed to persuade most Americans. They argue that greens need to develop more convincing arguments to get Americans to take global warming more seriously.

Predictably, Messrs Shellenberger and Nordhaus have unleashed a stream of counter-attacks that have led to a lively debate among American environmentalists. They conclude: “We in the environmental community today find ourselves head-down and knee-deep in the global warming river. It's time we got back to shore and envisioned a new path for the crossing.” Despite the

arrival of Kyoto, the debate and dissent of recent weeks suggests that the treaty has not produced the world of self-confident greens and smothered critics feared by Dr Crichton. In fact, the contrary seems to be true.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Land-use change

Animal, farm

Feb 3rd 2005 | PARIS
From The Economist print edition

New data are finally revealing global patterns of habitat loss

WHEN economists, scientists and governments want to study the state of the environment, and reach sensible decisions, they have a problem. Most of the data available concern local areas or regions, so it is difficult to get a global picture. But in late January, provisional data from the Millennium Ecosystem Assessment (MEA), an international effort launched by the United Nations in 2001, were presented to a conference on biodiversity, held in Paris.

Georgina Mace, of the Institute of Zoology in London, told the meeting that each year, 0.5% of the area of natural habitats on land is lost, largely due to conversion to farmland. The rate is consistent across most of the world's major “biomes”—such as grasslands, boreal forest and tropical moist forest. Furthermore, Dr Mace said, such losses look set to continue.

Within the 14 different terrestrial biomes the study identified, most have been greatly modified by humans. Between 20% and 50% of nine biomes have been transformed into croplands. Tropical dry forests are the worst hit, while 35% of temperate grasslands and broadleaf and Mediterranean forests have been converted.

What makes the MEA particularly interesting is that the goal of the overall report, due out in March, is to give a picture of how changes to the environment affect humans through degradation of the services that it provides. These would include things like watershed protection, pollination and protection from coastal erosion.

The report will differ from efforts to determine how much biological diversity a region holds. This is because an area may have many rare species, but not enough living matter to, say, prevent a coastline from being eroded. The starkest findings from the MEA, though, are to be expected in oceans. On land, the huge patterns of habitat loss have been offset by gains in food production. In water, though, the story is very different. Not only is there dramatic evidence of damage to marine ecosystems, but this has not been offset by similar gains in productivity.

There is a phrase that says what matters gets measured. It thus seems odd that nobody had yet done this kind of audit. The resulting lack of information seems to have led to the true value of many ecosystems being ignored or underestimated. Perhaps later this year the MEA will prove the opposite also to be true, that what is measured starts to matter.

Neuroscience

Quieting the brain, opening the mind

Feb 3rd 2005
From The Economist print edition

A drug-free treatment for epilepsy?

NEURONS—commonly known as nerve cells—communicate using electrical signals. However, sometimes communication is drowned out by more intense electrical signals, caused when each neuron continually excites and influences its neighbours.

This collective activity, known as bursting, has been recognised by neuroscientists for more than a decade. Sometimes it is beneficial—for example to help the correct neural connections to form in young brains. Sometimes, though, it is less benign. Epileptic fits appear to be neural bursts that have run out of control. Such fits can currently be controlled only by drugs. However, an attempt to link nerve cells directly to computers may be about to change that, by allowing the bursts associated with epileptic fits to be controlled directly.

Daniel Wagenaar of Caltech, in Pasadena, and Steven Potter of Georgia Tech, in Atlanta, have been growing rat and mouse neurons on arrays of electrodes connected to a computer. The first idea was to use the neurons to control the computer. The researchers' hope was that the neurons would add an ability to learn to a computer program.

However,the experiment failed, largely because of bursting. So Mr Wagenaar, Dr Potter and another researcher at Georgia Tech, Radhika Madhavan, set out to defeat bursting. Their results, published recently in the *Journal of Neuroscience*, show that this is possible using electrical stimulation alone. After a series of experiments involving various numbers of electrodes and various frequencies of stimulation, they have found that using an array of 25 electrodes and a stimulation rate of 50 pulses a second produces the desired suppression, but only if the electrodes themselves are out of synch with each other. The best results of all are obtained when the response to one burst of stimuli is used to regulate the rate and voltage of the next. And, once bursting is suppressed this way, the neurons revert rapidly to normal behaviour.

To exploit the potential of this work, the researchers have just formed a collaboration with Robert Gross of the Emory School of Medicine, also in Atlanta. Dr Gross, a surgeon, is already skilled at implanting stimulating electrodes into human brains. The group hopes to implant electrodes that can detect electrical activity as well as stimulate it. That way, stimulation can be given when needed—when a fit is actually beginning—rather than all the time. If that works, it could transform the lives of epileptics who now have to live with debilitating doses of drugs.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Computer circuits

Barred and latched

Feb 3rd 2005
From The Economist print edition

A molecular replacement for the transistor?

SMALL may be beautiful, but it is also hard. This is the reality faced by those trying to make ever-smaller transistors, one of the key components of virtually all modern electronic devices. The laws of physics place a limit on how small they can become.

This, then, is a tricky problem for those hoping to build future generations of computer chips that are vastly more powerful than today's. (The slow speed of electrical signals means that smaller components make for faster computers.) So the search has been on for a new type of architecture that will work in the tiny dimensions of the future. In a paper published this week in the *Journal of Applied Physics*, researchers from Hewlett-Packard's laboratories in Palo Alto, California, suggest they may have cracked part of the problem.

To understand the problem at hand, one might imagine a transistor as a sandwich. An electrical signal will pass across the three layers of the sandwich only if a small current is applied to the filling. So a transistor can be switched on or off with this control current. The problem with such a design is that, as the sandwich shrinks, the gap between the top and bottom layers gets so small that current tends to flow spontaneously across it.

Hewlett-Packard's researchers have been tinkering in a new area known as molecular electronics. Instead of using light to etch a transistor circuit on a wafer of silicon, they propose to fabricate tiny wires. The molecular-scale alternative proposed to the transistor is called a “crossbar latch”. The latch works by running an electrical current down a signal wire, through two switches. Controlling the voltage (the quantity of energy possessed by electrons moving down the wire) on the switches allows the latch to either work as an amplifier, restoring a signal to full strength, or as an inverter, converting a “1” to a “0”.

Because components to do things like logical “AND” operations (which returns a logical “1” only if it has two “1”s as input) already exist on the nanoscale, Phil Kuekes, one of the paper's authors, says the crossbar latch is the final piece of the puzzle necessary to build a molecular scale computer—something Hewlett-Packard's researchers plan to attempt next. They are, of course, not the only ones trying. The race to shrink electronic circuits will continue, even if and when the transistor falls by the wayside.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The Richard Casement internship

Feb 3rd 2005
From The Economist print edition

We invite applications for the 2005 Richard Casement internship. This is for a would-be journalist under 25 to spend three months of the summer on the newspaper, writing about science and technology. Our aim is more to discover writing talent in a science student than scientific aptitude in a budding journalist. Applicants should write a letter introducing themselves, along with an original article of about 600 words which they think would be suitable for publication in the Science and technology section. They should be prepared to come for an interview in London or New York, at their own expense. Applications must reach us by February 21st. They should be sent by e-mail to casement@economist.com

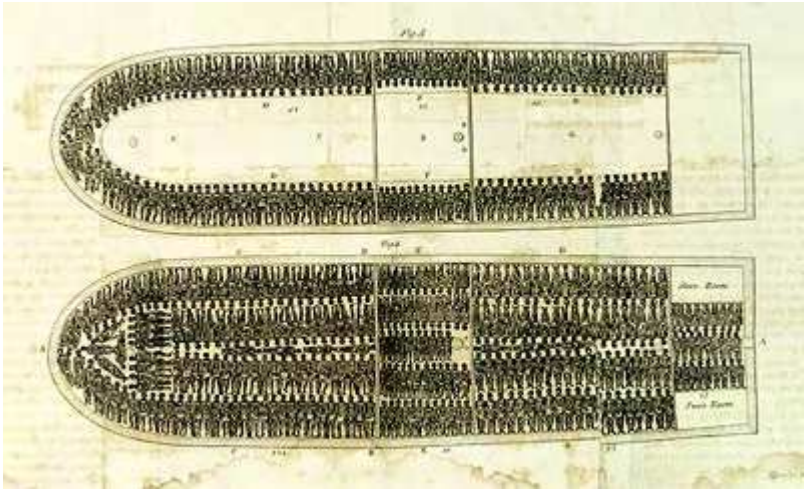
Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Slavery

Cruellest trade

Feb 3rd 2005
From The Economist print edition

Bridgeman



How a minority of abolitionists won over the majority

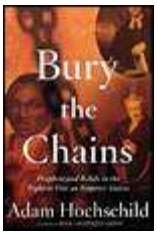
Get article background

DESPITE its gruelling subject matter, Adam Hochschild's study of colonial atrocities in the Belgian Congo of the late-19th century, “King Leopold's Ghost”, won praise and prizes. It was a story of official connivance at slavery and genocide, relieved by the presence of remarkable people who campaigned against it, notably Roger Casement and Edmund Morel. Now, in “Bury the Chains”, Mr Hochschild turns to an earlier and broader crusade for social justice, the movement to end the slave trade in the British empire. He spares us nothing of the awfulness of the Atlantic traffic and the cruelties that awaited slaves in the sugar plantations of the West Indies. But, as before, the book's true focus is the courage and moral clarity of the anti-slave campaigners. It is not an enjoyable read, but it is stirring and unforgettable.

Why an ancient practice, condemned neither by the New Testament nor by Christian tradition, was recognised as unacceptable by growing numbers of men and women in the second half of the 18th century has long puzzled historians. Mr Hochschild avoids big-picture answers and concentrates on the extraordinary characters involved.

His mainly British cast is a large one. It includes John Newton, a slave

Bury the Chains: Prophets and Rebels in the Fight to Free an Empire's Slaves
By Adam Hochschild



Houghton Mifflin; 468 pages; $26.95. Macmillan; £20

Buy it at
Amazon.com
Amazon.co.uk

Though the Heavens May Fall: The

captain who found God, rejected the trade and wrote, among many others, the hymn “Amazing Grace”; Granville Sharp, a musician and sponsor of lawsuits to free slaves in England; Olaudah Equiano, a freed slave and author of an autobiography that became the “Uncle Tom's Cabin” of the movement; Thomas Clarkson, an Oxford prize-winning Latinist and deacon of the Church of England who rode the country preaching abolition; and William Wilberforce, the tiny, evangelical member of parliament with a booming voice who piloted a slave-trade abolition bill through the House of Commons in 1807-08.

Landmark Trial that Led to the End of Human Slavery
By Steven Wise

Da Capo Press; 282 pages; $25. To be published in Britain by The Harvill Press in April 2006

Buy it at
Amazon.com
Amazon.co.uk

The objects of their concern were by no means all helpless victims. Slave rebellions rocked the West Indies throughout the 1790s and beyond. After the French abandoned Santo Domingo to the British in 1793, the army's attempt to put down Toussaint L'Ouverture's slave revolt cost more soldiers than it lost in the American war of independence. At Westminster, even MPs who approved of slavery questioned its expense.

Mr Hochschild has a chilling explanation for why British abolitionists concentrated on the slave trade. Unlike in the United States, where the slave population grew by natural increase, it would have fast vanished in British possessions but for “imports”. The sugar fields and refineries of the West Indies were so harsh that slaves died young and many female slaves were too weak to bear children. End the trade, the abolitionists reasoned, and slavery itself would die.

They were right about the tactic, wrong about timing. It was not until 1833 that slavery was finally outlawed in the British empire, although that was 30 years before the United States and more than 50 before the Spanish colonies. Abolitionists were needed to the end.

It once was fashionable to explain the ending of slavery as an economic consequence, and to treat changing attitudes as secondary. Slavery, it was argued, was ceasing to be profitable. With industrialisation, investors in slave ships and plantations had better places to put their money. Reformers, in effect, were pushing at an open door. Even if the dates worked better—and there was money in slavery well into the 19th century—mechanical stories of this kind would explain at best lack of resistance, not anti-slavery pressure.

Opponents of the slave trade agitated not only for new laws. They badgered courts to look at old law in fresh light. “Though the Heavens May Fall” by Steven Wise, an American lawyer concerned with animal and human rights, neatly complements Mr Hochschild's book. It gives a detailed account of legal challenges to slavery in Britain (but not the colonies), which culminated in the Somerset trial in 1772. James Somerset was a slave who had absconded while in England and whose master went to court to repossess him. The Lord Chief Justice, Lord Mansfield, ruled in Somerset's favour, denying the master's claims on the ground that in England, by established legal principle, everyone was free. Though Mansfield, somewhat contradictorily, sought to deny wider scope to his ruling, Granville Sharp and other abolitionists hailed it as the test case they had wanted. Masters of some 15,000 slaves in Britain seemed to agree: unsure of their owners' rights, many made slaves sign lifelong “apprenticeships”.

Both authors remind us how a committed minority can persuade a majority to see what at first they cannot or do not want to see. In one of many vivid passages, Mr Hochschild describes a simple but electrifying piece of evidence that Clarkson placed before an enquiry into the slave trade by the Privy Council in 1788. It was a diagram of a slave ship, the *Brookes*, showing slaves tightly packed and chained in rows. For many people, this was perhaps the first time that the reality of the slave trade had impinged upon them: with their own eyes, they could see its cruelty.

Bury the Chains: Prophets and Rebels in the Fight to Free an Empire's Slaves.
By Adam Hochschild.
Houghton Mifflin; 468 pages; $26.95. Macmillan; £20

Though the Heavens May Fall: The Landmark Trial that Led to the End of Human Slavery.
By Steven Wise.
Da Capo Press; 282 pages; $25. To be published in Britain by The Harvill Press in April 2006

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

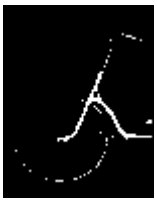
The bicycle

Cranium cracker

Feb 3rd 2005
From The Economist print edition

IT WAS no easy business to supplant the horse. A visionary Frenchman, Jacques Ozanam, first proposed a "self-moving vehicle" in 1696, but it was not until 1818 that a German eccentric, Baron Karl von Drais, produced a prototype for a vehicle that came to be known, with both love and hate, as the "velocipede". It was, in essence, a two-wheeled running machine without pedals. You sat astride it, you pushed yourself off, and you wore out the shoe leather. The clanking invention was mocked mercilessly by generations of caricaturists, and it does seem a little odd, even today, that it should have taken another half-century before the idea of pedals was hit upon.

Bicycle: The History
By David V. Herlihy



Yale University Press; 470 pages; $35 and £20

Buy it at
Amazon.com
Amazon.co.uk

The breakthrough came in 1867, when a French blacksmith named Michaux added not just pedals, but brakes. These first machines, made of solid iron, weighed in at over 30 kilos: unwieldy, they teetered on wooden wheels. Terrible anxieties about safety accompanied early expeditions. Some cyclists waxed lyrical about the joys of flying through the air. But not if you land head first, countered the rest. Bicycles were expensive, too, and only for toffs at first.

But sales boomed. In America, cycling rinks were built in most cities and championship races held. By the 1870s a new style was created, the so-called "high-wheeler", or "penny-farthing", as the American author of this history dutifully acknowledges it was called in Britain.

The move to the kind of cycle that we know and love today came in the 1880s, when Rover of Coventry in England produced a low-mount bicycle with chain drive and pedals. By 1890 Britain had half a million cycles on the road. Then Edouard Michelin invented the detachable tyre. Bliss was it in that dawn to be alive.

The history of the bicycle is also the story of its social acceptance as a fashionable mode of transport, and the impact that it had upon such things as items of dress. It obliged women, for example, to dress differently. "That women have legs, and that they are made for use, marks the beginning of a new era," a writer declared in the 1890s.

The cycle made a positive impact in other ways. It helped to pioneer road improvements. It was good for health. And the bicycle seeded other inventions: the Wright brothers and Henry Ford were bicycle mechanics before anything else. Above all, cycling seemed to foster a taste for travel and independence. As one contributor to *Outing* magazine put it in 1912: "you experience a re-birth of that forgotten sense of kinship with the birds."

This is the kind of feeling that drives along the author of this spirited, fast-moving, though occasionally overly nerdish, history of the machine that can take you so far for so little, give or

take a few minor bruises to thigh, ankle, leg, etc, etc.

Bicycle: The History.
By David V. Herlihy.
Yale University Press; 470 pages; $35 and £20

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Expressionist art

A fine line

Feb 3rd 2005 | FRANKFURT
From The Economist print edition

Some naked truths

AN EXCUSE to show erotic nudes in the name of art? Certainly, that is what the Viennese bourgeoisie believed around 1900, when Gustav Klimt, followed a few years later by Egon Schiele and Oskar Kokoschka, began to present the human figure stripped of its wrapping of mythology and allegory: a naked object of wonder, pity and maybe lust.

In your face

Now the Schirn Kunsthalle in Frankfurt has brought together some of the finest intimate, and occasionally erotic, works by these three painters, and a few others. It also aims to show the impact they had on turn-of-the-century Vienna, when the city was a place of Catholic prurience and rococo elegance.

When Klimt was commissioned to decorate a university hall with huge murals depicting medicine, jurisprudence and other disciplines, the professors expected the usual allegorical treatment, Instead, they got mostly naked women, whom they condemned as “ugly and immoral”. Klimt, indignant, bought back the paintings. He answered his critics with a life-size painting featuring a gorgeous woman whose bare behind is thrust into the face of the viewer. At the entrance of the exhibition, “Nuda Veritas”, a frontal nude holding a mirror, carries a quotation from Schiller: “It is bad to appeal to many.”

These artists of the so-called Vienna Secession certainly avoided that trap. They ran foul of the law: their publications were frequently confiscated. Schiele spent three weeks in custody for “sheltering” a 14-year-old girl who had run away from home. The court found him innocent of child abuse but guilty of hanging an obscene picture on his bedroom wall, which the magistrates deemed a “public place”.

Somehow, the Viennese failed to see what is apparent now: that Klimt and Schiele were among the finest ever draughtsmen of the female body. In Klimt, tenderness of line is at its most exquisite in a series of drawings in pencil and coloured crayon that are seldom shown because of their sensitivity to light. In Schiele, who came after Klimt, the line becomes tortured and more personal. There is less Art Nouveau in the use of colour and form.

Each of the Schiele paintings chosen by the curator, Tobias Natter, is a masterpiece: the nun and the cardinal on their knees kissing; mother and naked daughter in an embrace; a contorted life-size portrait of the artist—naked, of course—which would have been Mr Natter's choice for the catalogue cover had the publisher not decided it would go down badly in America and Japan. Even so, the viewer will conclude that the 200-or-so pictures on show are emphatically art rather than porn—even if some may cause blushes.

In 1910 Kokoschka left Vienna for Berlin and joined another radical movement, *Der Sturm*. Berlin may have been more tolerant, but he shocked the public with troubled pictures of himself and his wife. A disgusting puppet resembling her appears in many later paintings, first life-size then ever smaller. There are also pictures by other contemporaries, including Anton Kolig, a repressed homosexual whose drawings of young men, in the studio or on his alpine art courses, are full of power and tenderness. He let his pencil roam where his hands dared not go.

Who were the successors to the artists of the Vienna Secession? Francis Bacon, perhaps, or Lucien Freud. For contemporary purveyors of scandal, one might look among the sharks in formaldehyde and heads of frozen human blood. Yet these offer nothing to rival the mastery of line and form that distinguishes Klimt and Schiele from the rest.

"Die Nackte Wahrheit" is at the Schirn Kunsthalle until April 24th. It then moves to the Leopold Museum in Vienna from May 13th-August 22nd.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Ian McEwan

The thinker

Feb 3rd 2005
From The Economist print edition

IT IS 3.40 in the morning of Saturday February 15th 2003. Henry Perowne is standing at the bedroom window of his smart London home. Wondering why he has woken so early, he sees a plane with one of its engines on fire, streaking like a comet towards Heathrow airport. In a post-September 11th world this fills him with unease: “Everyone agrees, airliners look different in the sky these days, predatory and doomed.” This is the opening to “Saturday”, Ian McEwan's enthralling tenth novel.

Saturday
By Ian McEwan

Nan A. Talese/Doubleday; 279 pages; $26.00
Jonathan Cape; 279 pages; £17.99.

Buy it at
Amazon.com
Amazon.co.uk

The book is a product of a world where terrorism and war make headlines, but also filter into the smallest corners of people's lives. The action takes place on a single day—shades of “Ulysses” and “Mrs Dalloway”—when demonstrators mass on London's streets to protest at Britain's involvement in the imminent war in Iraq.

Unusually in fiction these days, the book's protagonist is happy. Perowne is a 48-year-old neurosurgeon—so successful, fulfilled and wealthy that he could come across as smug were he not so sensitively portrayed as a thoughtful man. Here is someone at the top of his game: at work “he was renowned for his speed, his success rate and his list”, while at home his marriage is strong and sexy and his relationship with his two children full of charm and chumminess.

Yet the personal happiness is counterbalanced by feelings of pessimism about the state of the world. He worries about the morality of the coming war (though he believes there is no viable alternative) and the likelihood of a terrorist attack on London. His family life, he feels, is under threat. The theme of impending catastrophe wrecking an idyll is vintage McEwan, and contributes both to the book's pace and tension.

The small nugget of a plot is that Perowne collides with another fate. On his way to a squash game, a minor car accident brings him into confrontation with Baxter, a twitchy, aggressive 20-something. Perowne sidesteps a beating, extricating himself from Baxter's clutches by correctly guessing that he is suffering from a neuro-degenerative disease. That evening, as the family gathers for a reunion, Baxter enters the house bent on revenge. Events tumble towards the denouement.

Mr McEwan is a writer of the highest talents, and this is an elegantly constructed novel. Readers might wonder, though, what it all adds up to: whether it tells you anything you do not already know. The author draws his characters with flair, and even those that are less shaded are still believable. Meanwhile, his prose—visually descriptive and intense—spells out the minutiae of daily life in a way that lends depth to the book.

But the juxtaposition of fiction against the realism of a 24-hour news cycle works less well. It is hard to see the relevance beyond creating a sense of place and time. “Saturday” is not a McEwan masterpiece: it is just a little too safe. But it is still hugely enjoyable for all that.

Saturday.
By Ian McEwan.
Jonathan Cape; 279 pages; £17.99.
To be published in America by Nan A. Talese in March 2005

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

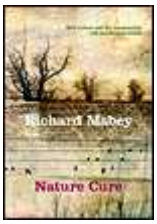
Richard Mabey

Healing force

Feb 3rd 2005
From The Economist print edition

A GOOD hobby flatters its practitioners by making them feel skilful. The best hobbies make them feel virtuous too, which is one reason why people get keen on ecological pastimes. Mixing a crafty compost from the kitchen waste, or locating a slightly edible mushroom in a suburban thicket, can burnish a green halo, and seem like striking a blow for global cooling or against genetic modification. That is ecology-lite, and for its British practitioners Richard Mabey is a bit of a guru. He calls his ecology “deep”, and writes about it elegantly.

Nature Cure
By Richard Mabey



Chatto & Windus; 232 pages; £15.99

Buy it at
Amazon.co.uk

Cruel nature does not reward its devotees. On finishing his valuable and curious “Flora Britannica”, Mr Mabey fell ill with the ultimate disorder of complicated societies, acute depression. He stared at the wall, unable to practise his recreation or his trade, to talk to a friend or pay a bill or manage his existence. He found himself in the hospital near Northampton where the marvellous and depressive rural poet John Clare was confined in the 1840s.

This little book tells how Mr Mabey (unlike poor Clare) came out of his depression. He fell in love, and his new love urged him again to look at and write about the green world. His home had gone, and he had to start all over again, making a living as a writer, a trade that he says is like being “alone in a room for a very long time, climbing without a rope.” Like Clare, he fashions his rope from observations of reality, exquisitely described.

Adversity only strengthened his refusal to understand what is meant by the “tragedy of the commons”. He even objects to his own temerity, in having owned and remodelled a neglected woodland that was the most precious of his lost possessions. His principle is resistance to “the modern world's project of appropriating and taming nature, of turning it into an object”. Yet he finds his new home where nature has been most thoroughly objectified by subsidised farming, the grain-and-beet land of East Anglia.

Even there he finds lingering plants and small deer, and birds whose miraculous migrations connect him to the Arctic, to Africa, and across time to the paintings that Europe's human discoverers left in caves. His private devotion is to swifts, those high-screeching insectivores that stop flying only to breed and fly again. “The birds don't give a fig about me or any of us,” he says in praise.

An American trip changes things. Mr Mabey finds suburbs cheek-by-jowl with landscapes that man has not created and is indifferent to; sheer wildness disorients him, even when deliberately restored. Back home, his glimpse of vastness “made me look at our own tamed acres with a new respect, and a willingness to suspend judgement about their domesticity.” He ventures on to East

Anglia's vast, flat factory farms, and finds, as colossal machines trundle in the harvest, that the sky is crammed with multifarious birds.

Nature Cure.
By Richard Mabey.
Chatto & Windus; 232 pages; £15.99

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Amazon worldwide bestsellers

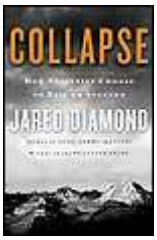
The big book index

Feb 3rd 2005
From The Economist print edition

The bestselling history titles in January

HISTORY is ever more broadly defined, as January's list of bestselling history books from Amazon websites shows. The collapse of societies, the Holocaust and George Washington are some of the disparate subjects recently to have grabbed readers' attentions.

1. Collapse: How Societies Choose to Fail or Succeed.
By Jared Diamond. *Viking; 592 pages; $20. Penguin/Allen Lane; £29.95*



Jared Diamond, a geographer at the University of California, focuses on long-term environmental factors rather than short-term political ones to find out why societies fail.

Click to buy from Amazon.com or Amazon.co.uk

2. 102 Minutes: The Untold Story of the Fight to Survive Inside the Twin Towers.
By Jim Dwyer and Kevin Flynn. *Times Books; 352 pages; $26*

An account of the struggle for life inside the World Trade Centre on September 11th.

Click to buy from Amazon.com or Amazon.co.uk

3. Guns, Germs and Steel: The Fates of Human Societies.
By Jared Diamond. *Norton; 480 pages; $16.95. Vintage; £8.99*

Jared Diamond's previous long view of what leads to the rise of civilisations.

Click to buy from Amazon.com or Amazon.co.uk

4. Auschwitz: The Nazis and the Final Solution.
By Laurence Rees. *PublicAffairs; 327 pages; $30. BBC Books; £20*

Published to commemorate the 60th anniversary of Auschwitz's liberation, the book attempts to explain how the Final Solution could possibly have been dreamt up.

Click to buy from Amazon.com or Amazon.co.uk

5. The Holy Blood and the Holy Grail.
By Michael Baigent. *Dell; 67 pages; $7.99. Arrow; £8.99*

A book stating that Jesus may have lived to marry and have children. Not Monty Python.

Click to buy from Amazon.com or Amazon.co.uk

6. Anne Frank Tagebuch.
By Anne Frank. *Fischer; 263 pages; €59*

The famous diary, in German, of Anne Frank, who died as a young girl at Bergen-Belsen.

Click to buy from Amazon.de

7. His Excellency: George Washington.
By Joseph J. Ellis. *Knopf; 352 pages; $26.95*

A new, and short, biography of America's first president based on his personal papers.

Click to buy from Amazon.com or Amazon.co.uk

8. The Case for Democracy: The Power of Freedom to Overcome Tyranny and Terror.
By Natan Sharansky. *PublicAffairs; 320 pages; $26*

A former Soviet political prisoner and then Israeli politician explains why democracy is not beyond the reach of any nation.

Click to buy from Amazon.com or Amazon.co.uk

9. Deutschland: Der Abstieg eines Super-stars.
By Gabor Steingart. *Piper; 320 pages; €13*

Germany: Decline of a Super Star anguishes over the country's turns since 1945 though what preceded it was presumably worse.

Click to buy from Amazon.de

10. In the Footsteps of Mr Kurtz: Living on the Brink of Disaster in Mobutu's Congo.
By Michela Wrong. *Perennial; 336 pages; $11.16. Fourth Estate; £7.99*

A powerful tale of disintegration in mineral-rich Congo.

Click to buy from Amazon.com or Amazon.co.uk

11. Who Do You Think You Are?
By Dan Waddell. *BBC Books; 192 pages; £12.99*

How to trace your ancestors.

Click to buy from Amazon.co.uk

12. Dreams From My Father: A Story of Race and Inheritance.
By Barack Obama. *Three Rivers Press; 480 pages; $13.95*

A memoir by the new young and black senator for Illinois brought up in Hawaii and Indonesia.

Click to buy from Amazon.com or Amazon.co.uk

Source: Global sales from Amazon.com, Amazon.co.uk, Amazon.ca, Amazon.de, Amazon.fr and Amazon.jp, from December 27th 2004-January 28th 2005. Prices are quoted from Amazon.com and Amazon.co.uk, and are correct as of January 28th.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com PEOPLE
PRINTABLE PAGE VIEW SPONSORED BY

Obituary

Miriam Rothschild

Feb 3rd 2005
From The Economist print edition

Getty Images

Dame Miriam Rothschild, a scientist of the old style, died on January 20th, aged 96

IN A typically generous moment, Miriam Rothschild once named a flea after a writer on *The Economist*. He had fortuitously helped to discover a new one on a zoological expedition in Africa. The gesture was probably the highest honour she could bestow on anyone.

She thought fleas beautiful. Gazing at their stained sections through the microscope, she once said, gave her a feeling as ecstatic as smoking cannabis. In her bedroom she kept them in cellophane bags, in order not to miss a thing that they were doing. She had discovered, by watching thousands of them jump, that they were actually adapted for flight, and that the jumping flea developed an acceleration on take-off 20 times that of a moon rocket re-entering the Earth's atmosphere. A lifelong atheist, she admitted that she had been tempted to believe in a creator when she discovered that the flea had a penis.

Her fascination had begun young, on holiday in Transylvania, when her father had allowed her to help him catch fleas from a mouse. Already, in the sprawling Rothschild family seat where she was brought up and informally schooled, Miriam had a collection of ladybirds and butterflies, the butterflies pinned on card by herself. But her father was a flea man. He and her uncle Walter had already established, at Tring in Hertfordshire, the largest private natural history collection in Britain: 200,000 birds' eggs, 300,000 bird skins, 144 giant tortoises that wandered in the grounds, more than 2m butterflies, and plenty of fleas. These included 12 dressed fleas from Mexico, with a couple garbed like a bride and groom.

Her father's obsession with fleas, however, was not a dilettante enthusiasm, but a serious scientific interest. He had identified the flea that carries plague, *Xenopsylla cheopis Rothschild*, and had written more than 150 papers on the creatures. His daughter followed him into the depths of parasitology. It was not a glamorous field. As she noted ruefully in her book “Fleas, Flukes and Cuckoos”, a popular study of parasitism, “Birds' fleas and feather lice do not sing. Nor do they fly about flashing brilliantly coloured wings in the sunshine...The collectors of fleas and lice can be counted on the fingers of one hand!” Yet she loved them. Her life's work, which took 30 years and filled six volumes, was to catalogue her father's collection.

Nor did she stop there. As a passionate enthusiast for all living creatures (except some irritating humans), she produced more than 300 scientific papers over the years. She did special research into a parasite that lived only in the eyelashes of hippopotami. She studied the behaviour of black-headed gulls, buying gull-eggs in Leadenhall market in order to incubate them herself and put them in her aviary. During the second world war she tracked the role of wood pigeons in transmitting TB to cattle and, as she lurked in the fields with her crate of birds, was once taken for a German spy. She discovered that monarch butterflies absorbed toxins from milkweed in order to use them, as the plant did, for defence. She was most fascinated by the role of pyrazines, or aromas, in the lives of insects, pointing out that each species of butterflies and moths had its own distinctive scent. The smell of a very gently squeezed ladybird, she once said, “will stay on your hands for days”.

A natural philosopher

As the years passed, this passionate scientist, who had never taken a degree and lived most of the time on the farm where she had been born, accumulated eight honorary doctorates. She became a Fellow of the Royal Society and of St Hugh's College, Oxford. These honours were not always given without grumbles from the men in the labs. In an age of intense specialisation and professionalism in science, she appeared as a happy amateur and generalist. She was, in fact, a throwback to a different age, when gentlemen of means (and the Rothschilds had plenty of those) set up their own home laboratories and cabinets of curiosities, and pursued science for the sheer joy of it.

She also had a view of science that was unashamedly broad, taking in arts, literature and natural philosophy—much in the mould of Erasmus Darwin at the end of the 18th century, whose tomes on botany and zoology were written in Wordsworthian verse. Very early, she was a part of the environmental movement and an exponent of the “web of life” theory, in which all species in an area depend on each other and on the preservation of habitat. Visitors to her farm in Northamptonshire found it a riot of weeds and wild flowers, a style she impressed on the Prince of Wales at Highgrove. She herself moved through the gardens like a ship in full sail, dressed in her favourite purple or sea-green gowns. Since she had eschewed leather on principle (together with meat and alcohol), she would sometimes wear white wellingtons for evening.

Perhaps the most pleasing image of her, though, was the one that appeared in the Latin citation for her honorary degree from Oxford in 1968. “She has come to this our Capitol”, it read, “not by degrees, but by one leap as of her fleas, in a triumphal chariot...drawn not by Venus's doves, Juno's peacocks, Alexander's gryphons or Pompey's elephants, but by her sixty-odd species of avian parasites.”

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Overview

Feb 3rd 2005
From The Economist print edition

America's economy grew by a slower-than-expected 3.1% at an annual rate in the fourth quarter, compared with 4.0% in the third quarter. The Federal Reserve put up its key interest rate by one-quarter of a percentage point to 2.5%.

Inflation in America remains restrained. According to one measure favoured by the Federal Reserve, core personal-consumption prices, which exclude the volatile prices of food and energy, rose by 1.7% in the year to December. Personal incomes rose by 3.7% in December, owing mostly to a one-time $32 billion dividend from Microsoft. Excluding the effects of the dividend, income rose by 0.6%. Sales of new homes in America in December were lower than expected at 1.1m.

The **euro area's** economic sentiment indicator rose slightly in January to 100.6 from 100.2 in December. In **Germany**, the number of unemployed rose yet again in January to just over 5m, a post-war record high. Retail sales fell by 5.9% in the year to December. In **Austria**, industrial production rose by 8.5% in the year to November.

Industrial production in **Canada** rose by 3.8% in the year to November.

In **Japan**, industrial production rose by 1.4% and consumer prices rose by 0.2% in the year to December. The unemployment rate fell in December to 4.4% from 4.5% in the previous month.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Output, demand and jobs

Feb 3rd 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2004	2005	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 3.0	Q3	+ 1.2	+ 3.6	+ 3.0	+ 4.2	Q3	+ 5.7	Q3	5.1	Dec	5.8
Austria	+ 2.7	Q3	+ 3.2	+ 1.7	+ 2.1	+ 8.5	Nov	– 2.9	Oct	4.5	Jan	4.5
Belgium	+ 2.9	Q3	+ 3.2	+ 2.5	+ 2.1	+ 3.0	Nov	– 0.8	Oct	12.8	Dec†	12.7
Britain	+ 2.8	Q4	+ 3.0	+ 3.2	+ 2.4	– 0.9	Nov	+ 3.2	Dec	4.7	Nov††	4.9
Canada	+ 3.3	Q3	+ 3.2	+ 2.8	+ 3.1	+ 3.8	Nov	+ 5.0	Oct	7.0	Dec	7.4
Denmark	+ 1.8	Q3	+ 0.5	+ 2.1	+ 2.0	– 1.6	Nov	+ 9.8	Dec	6.2	Dec	6.7
France	+ 1.9	Q3	– 0.1	+ 2.1	+ 1.8	+ 2.1	Nov	+ 3.5	Nov	9.9	Dec	9.9
Germany	+ 1.3	Q3	+ 0.4	+ 1.3	+ 1.2	– 0.2	Nov	– 5.9	Dec	11.4	Jan§	10.2
Italy	+ 1.3	Q3	+ 1.7	+ 1.2	+ 1.5	– 2.8	Nov	– 3.5	Oct	7.7	Jun	8.6
Japan	+ 2.6	Q3	+ 0.2	+ 3.2	+ 1.6	+ 1.4	Dec	+ 0.3	Nov	4.4	Dec	4.9
Netherlands	+ 1.5	Q3	+ 1.3	+ 1.2	+ 1.2	– 0.7	Nov	– 2.6	Oct‡	6.5	Dec**	5.7
Spain	+ 2.6	Q3	+ 2.4	+ 2.6	+ 2.4	+ 4.0	Nov	+ 3.2	Nov	10.4	Dec	11.2
Sweden	+ 3.9	Q3	+ 3.8	+ 3.4	+ 2.8	+ 1.2	Nov	+ 4.8	Dec	5.6	Dec†	5.1
Switzerland	+ 1.8	Q3	+ 1.4	+ 1.8	+ 1.8	+ 3.5	Q3	+ 3.9	Nov	4.0	Dec†	4.1
United States	+ 3.7	Q4	+ 3.1	+ 4.4	+ 3.5	+ 4.4	Dec	+ 5.9	Dec	5.4	Dec	5.7
Euro area	+ 1.8	Q3	+ 1.1	+ 1.8	+ 1.6	+ 0.5	Nov	+ 0.4	Nov	8.9	Dec	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 3.2	Q3	+ 4.3	na	na	+12.0	Dec	+ 4.0	Nov	7.7	Dec†	8.2
Greece	+ 3.8	Q3	na	na	na	+ 2.8	Nov	+ 6.3	Oct	10.7	Mar	9.8
Iceland	+ 7.4	Q3	na	na	na	na		na		2.7	Dec†	3.4
Ireland	+ 5.8	Q3	na	na	na	–10.4	Nov	+ 4.2	Nov	4.2	Dec	4.4
Luxembourg	+ 2.12003		na	na	na	+ 5.2	Oct	+ 5.4	Nov	4.5	Dec	4.2
New Zealand	+ 4.0	Q3	+ 1.9	na	na	+ 4.5	Q3	+ 7.4	Q3	3.8	Q3	4.4
Norway	+ 1.8	Q3	– 3.9	na	na	+ 0.9	Nov	+ 3.3	Nov	4.1	Jan‡	4.3
Portugal	+ 0.8	Q3	– 4.9	na	na	– 2.1	Dec	+ 5.2	Dec	6.8	Q3†	6.1

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Sep-Nov; claimant count rate 2.7% in Dec. §EU harmonised rate 10.0% in Dec. **Oct-Dec.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Prices and wages

Feb 3rd 2005
From The Economist print edition

% change on year ago

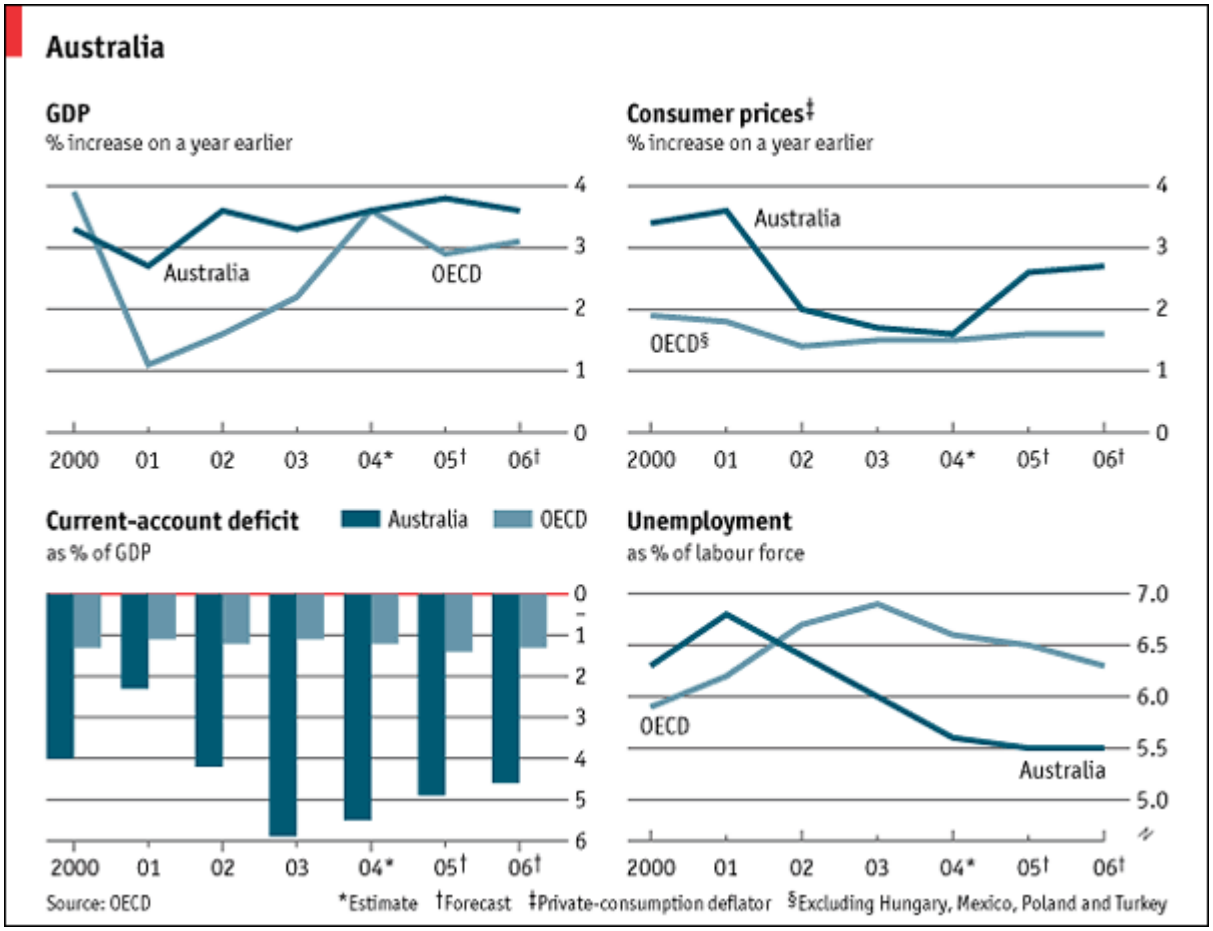
	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2004	The Economist poll consumer prices forecast 2005	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 2.6	Q4	+ 2.4	+ 2.3	+ 2.5	+ 8.2	Q4	– 1.1	+ 3.7	Q3	+ 5.1
Austria	+ 2.9	Dec	+ 1.2	+ 2.0	+ 1.7	+ 5.2	Dec	+ 2.5	+ 2.0	Dec	+ 2.3
Belgium	+ 2.3	Jan	+ 1.6	+ 2.1	+ 1.7	+ 5.3	Dec	– 0.4	+ 2.4	Oct	+ 1.8
Britain	+ 1.6	Dec*	+ 1.3	+ 1.5	+ 1.7	+ 2.9	Dec	+ 1.8	+ 4.2	Nov†	+ 3.6
Canada	+ 2.1	Dec	+ 2.0	+ 1.9	+ 2.1	+ 4.1	Nov	– 4.1	+ 2.3	Oct	+ 3.2
Denmark	+ 1.2	Dec	+ 1.4	+ 1.2	+ 1.6	+ 2.7	Dec	+ 0.2	+ 2.9	Q3	+ 3.7
France	+ 2.1	Dec	+ 2.2	+ 2.2	+ 1.6	+ 3.0	Dec	+ 0.3	+ 2.7	Q3	+ 2.9
Germany	+ 1.6	Jan	+ 1.2	+ 1.8	+ 1.3	+ 3.8	Dec	+ 1.2	+ 0.3	Nov	+ 0.6
Italy	+ 2.0	Dec	+ 2.5	+ 2.3	+ 2.0	+ 4.2	Dec	+ 0.8	+ 3.3	Dec	+ 2.7
Japan	+ 0.2	Dec	– 0.4	– 0.1	nil	+ 1.9	Dec	– 0.2	– 0.5	Dec	+ 3.0
Netherlands	+ 1.2	Dec	+ 1.7	+ 1.3	+ 1.2	+ 5.6	Nov	+ 1.1	+ 0.9	Dec	+ 2.4
Spain	+ 3.2	Dec	+ 2.6	+ 3.0	+ 2.8	+ 5.0	Dec	+ 1.1	+ 2.2	Q3	+ 3.1
Sweden	+ 0.4	Dec	+ 1.4	+ 0.7	+ 1.5	+ 2.0	Dec	– 1.9	+ 2.4	Nov	+ 3.4
Switzerland	+ 1.2	Jan	+ 0.2	+ 0.8	+ 1.2	+ 1.5	Dec	– 0.2	+ 1.4	2003	+ 1.8
United States	+ 3.3	Dec	+ 1.9	+ 2.7	+ 2.4	+ 4.1	Dec	+ 3.7	+ 2.7	Dec	+ 1.8
Euro area	+ 2.4	Dec	+ 2.0	+ 2.1	+ 1.8	+ 3.6	Dec	+ 1.0	+ 2.0	Q3	+ 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.4	Dec	+ 0.6	na	na	+ 0.7	Dec	– 0.4	+ 3.1	Q3	+ 4.3
Greece	+ 3.1	Dec	+ 3.1	na	na	+ 2.6	Nov	+ 2.6	na		na
Iceland	+ 4.0	Jan	+ 2.4	na	na	+ 8.6	Jan	+ 1.3	+ 6.0	Dec	+ 5.4
Ireland	+ 2.6	Dec	+ 1.9	na	na	– 1.6	Dec	– 9.1	+ 4.5	Q3	+ 4.6
Luxembourg	+ 2.2	Dec	+ 2.1	na	na	+15.7	Nov	+ 1.1	– 2.5	Oct	na
New Zealand	+ 2.7	Q4	+ 1.6	na	na	+ 2.5	Q3	+ 0.1	+ 2.2	Q3	+ 2.3
Norway	+ 1.1	Dec	+ 0.6	na	na	+ 9.7	Dec	+ 0.7	+ 4.6	Q3	+ 4.2
Portugal	+ 2.5	Dec	+ 2.4	na	na	+ 4.7	Dec	nil	+ 2.2	Nov	– 1.6

*New series. RPI inflation rate 3.5% in Dec. †Sep-Nov.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Australia

Feb 3rd 2005
From The Economist print edition



The Australian economy has been on a winning streak since the early 1990s. It has enjoyed 13 years of uninterrupted growth, the longest expansion in Australia since 1945. The winning streak is set to continue over the next two years, says the OECD. It expects GDP to increase by 3.8% in 2005 and by 3.6% in 2006. Despite this hefty growth, inflation is forecast to keep within the target band of 2-3% a year. The current-account deficit is forecast to decline from 5.5% of GDP in 2004 to 4.6% in 2006. The main risk to the economic outlook is that heavily indebted households may save more and spend less than expected. Debt-servicing payments are higher in relation to disposable income than at their previous peak in the late 1980s. However, the OECD thinks that a soft landing is likely both for the housing market and consumer spending.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Money and interest rates

Feb 3rd 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Feb 2nd 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 2.6	+ 9.2	Dec	5.47	5.58	5.22	5.32	5.69	6.19
Britain	+ 5.8	+ 8.6	Dec	4.83	4.13	4.50	4.58	4.85	5.24
Canada	+11.2	+10.4	Dec	2.43	2.27	2.92	4.31	4.56	5.65
Denmark	+14.4	+12.7	Dec	2.25	2.15	2.40	3.60	4.31	5.05
Japan	+ 4.1	+ 2.0	Dec	0.02	0.03	0.09	1.29	1.28	1.37
Sweden	– 0.2	+ 4.6	Dec	1.98	2.51	2.15	3.70	4.58	2.19
Switzerland	– 5.3	+ 1.2	Dec	0.75	0.24	0.89	2.07	2.52	2.19
United States	+ 5.4	+ 6.2	Dec	2.60	1.02	3.31	4.14	4.27	5.36
Euro area†	+ 8.4	+ 6.4	Dec	2.14	2.09	2.38	3.51	4.14	3.70

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.58%, Japan No. 266 1.27%. Central bank rates: US fed funds 2.50%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.75%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The Economist commodity price index

Feb 3rd 2005
From The Economist print edition

1995=100

	Jan 25th	Feb 1st*	% change on one month	% change on one year
Dollar index				
All items	90.0	90.6	+ 1.5	– 1.5
Food	82.7	82.0	– 0.1	– 7.9
Industrials				
All	99.9	102.1	+ 3.3	+ 6.7
Nfa†	84.9	86.9	+ 5.0	– 5.4
Metals	112.7	115.0	+ 2.3	+16.1
Sterling index				
All items	76.2	76.0	+ 1.8	– 3.7
Euro index				
All items	91.4	91.6	+ 3.8	– 4.9
Yen index				
All items	99.7	100.3	+ 1.3	– 2.7
Gold				
$ per oz	423.50	420.10	– 1.4	+ 4.2
West Texas Intermediate				
$ per barrel	49.64	47.16	+11.8	+38.0

* Provisional. † Non-food agriculturals.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Stockmarkets

Feb 3rd 2005
From The Economist print edition

Market indices

		2004-05		% change on one week	% change on record high	% change on Dec 31st 2003 in local currency	% change on Dec 31st 2003 in $ terms
	Feb 2nd	high	low				
Australia (All Ordinaries)	4,141.2	4,141.2	3,274.9	+ 2.1	nil	+25.3	+28.7
Austria (ATX)	2,522.4	2,522.4	1,568.9	+ 1.4	nil	+63.2	+68.7
Belgium (Bel 20)	3,027.4	3,027.4	2,244.2	+ 0.6	-17.8	+34.9	+39.4
Britain (FTSE 100)	4,916.2	4,916.2	4,287.0	+ 1.4	-29.1	+ 9.8	+15.6
Canada (Toronto Composite)	9,303.9	9,303.9	8,123.5	+ 1.5	-18.3	+13.2	+17.9
Denmark (KBX)	267.1	267.1	219.0	+ 2.5	-11.5	+25.0	+29.3
France (SBF 250)	2,735.7	2,735.7	2,386.1	+ 1.9	-37.7	+13.4	+17.2
(CAC 40)	3,951.7	3,951.7	3,465.3	+ 1.9	-42.9	+11.1	+14.8
Germany (DAX)	4,296.3	4,316.4	3,647.0	+ 2.0	-46.7	+ 8.4	+12.0
Italy (BCI)	1,523.6	1,516.1	1,239.5	+ 1.2	-30.2	+21.2	+25.3
Japan (Nikkei 225)	11,407.1	12,163.9	10,365.4	+ 0.3	-70.7	+ 6.8	+10.2
(Topix)	1,152.0	1,217.9	1,022.6	+ 0.6	-60.1	+10.4	+13.9
Netherlands (AEX)	365.5	365.5	310.7	+ 2.5	-47.9	+ 8.2	+11.9
Spain (Madrid SE)	992.7	992.7	804.4	+ 2.7	-13.4	+22.9	+27.0
Sweden (Affarsvarlden Gen)	226.4	226.4	188.5	+ 2.1	-43.5	+20.2	+24.1
Switzerland (Swiss Market)	5,795.1	5,934.4	5,309.7	+ 0.5	-31.1	+ 5.6	+ 9.6
United States (DJIA)	10,596.8	10,854.5	9,750.0	+ 0.9	- 9.6	+ 1.4	+ 1.4
(S&P 500)	1,193.2	1,213.6	1,063.2	+ 1.6	-21.9	+ 7.3	+ 7.3
(NASDAQ Comp)	2,075.1	2,178.3	1,752.5	+ 1.4	-58.9	+ 3.6	+ 3.6
Europe (FTSEurofirst 300)*	1,073.6	1,073.6	940.9	+ 1.8	-37.0	+12.1	+15.8
Euro area (FTSE Euro 100)*	922.9	922.9	787.2	+ 2.1	-40.5	+11.0	+14.7
World (MSCI)†	1,152.7	1,170.0	997.0	+ 1.3	-20.4	+11.2	+11.2
World bond market (Citigroup)‡	656.4	666.7	575.1	- 0.2	- 1.5	+ 8.7	+ 8.7

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms.
‡Citigroup World Government Bond Index, total return, in $ terms.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Trade, exchange rates and budgets

Feb 3rd 2005
From The Economist print edition

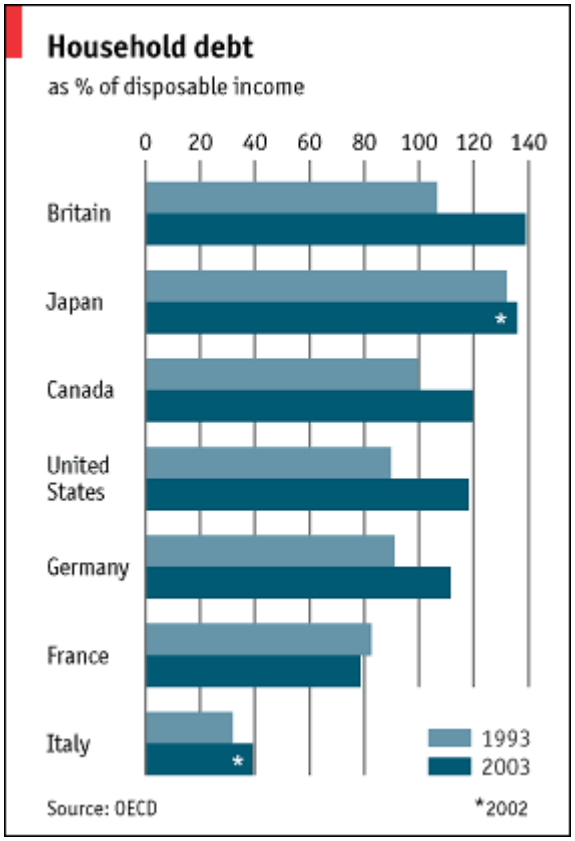
	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2004	2005	Exchange rate trade-weighted† 1990=100 Feb 2nd	year ago	Currency units per $ Feb 2nd	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2004‡
Australia	− 18.0	Dec	− 36.2	Q3	− 6.0	− 5.4	87.6	88.0	1.29	1.32	2.43	1.68	1.24	+ 0.7
Austria	+ 0.5	Nov	− 1.8	Nov	− 0.6	− 0.7	103.4§	102.8	0.77	0.80	1.45	–	0.74	− 1.5
Belgium	+ 21.4	Nov	+ 11.7	Sep	+ 3.6	+ 3.4	104.0§	102.9	0.77	0.80	1.45	–	0.74	− 0.1
Britain	−104.0	Nov	− 47.4	Q3	− 2.4	− 2.6	103.0	103.4	0.53	0.55	–	0.69	0.51	− 3.2
Canada	+ 52.8	Nov	+ 26.7	Q3	+ 2.8	+ 2.2	92.1	86.0	1.24	1.34	2.34	1.62	1.19	+ 1.1
Denmark	+ 9.5	Nov	+ 5.9	Nov	+ 2.9	+ 2.6	107.0	106.9	5.71	5.95	10.8	7.44	5.50	+ 0.9
France	− 6.0	Nov	− 3.4	Nov	+ 0.1	+ 0.1	107.6§	106.3	0.77	0.80	1.45	–	0.74	− 3.7
Germany	+192.7	Nov	+ 95.9	Nov	+ 3.1	+ 2.9	105.4§	103.9	0.77	0.80	1.45	–	0.74	− 3.9
Italy	+ 0.3	Nov	− 12.0	Nov	− 0.8	− 0.9	76.7§	75.8	0.77	0.80	1.45	–	0.74	− 2.9
Japan	+131.7	Nov	+167.7	Nov	+ 3.3	+ 3.4	137.7	138.1	104	106	196	135	–	− 6.5
Netherlands	+ 36.6	Nov	+ 21.0	Q3	+ 3.0	+ 3.0	103.6§	102.3	0.77	0.80	1.45	–	0.74	− 2.9
Spain	− 72.5	Nov	− 43.3	Oct	− 3.7	− 3.9	77.8§	77.0	0.77	0.80	1.45	–	0.74	− 1.1
Sweden	+ 22.9	Dec	+ 26.2	Q3	+ 7.6	+ 6.7	82.6	81.4	6.97	7.34	13.1	9.08	6.71	+ 0.5
Switzerland	+ 8.0	Dec	+ 44.7	Q3	+12.4	+11.9	112.7	110.9	1.19	1.25	2.25	1.55	1.15	− 1.6
United States	−653.8	Nov	−603.2	Q3	− 5.5	− 5.6	91.2	95.0	–	–	1.88	1.30	0.96	− 4.4
Euro area	+ 93.9	Nov	+ 48.3	Nov	+ 0.5	+ 0.5	93.0	91.8	0.77	0.80	1.45	–	0.74	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 12.8	Nov	+ 6.9	Nov	na	na	82.7§	81.6	0.77	0.80	1.45	–	0.74	+ 2.3
Greece	− 31.2	Nov	− 10.0	Nov	na	na	60.0§	59.4	0.77	0.80	1.45	–	0.74	− 5.3
Iceland	− 0.8	Nov	− 0.6	Q3	na	na	96.1**	93.0	61.6	69.0	116	80.2	59.3	+ 0.1
Ireland	+ 41.8	Nov	− 1.6	Q3	na	na	96.3§	94.5	0.77	0.80	1.45	–	0.74	+ 0.2
Luxembourg	− 4.4	Nov	+ 2.3	Q3	na	na	104.0§	102.9	0.77	0.80	1.45	–	0.74	− 0.4
New Zealand	− 2.8	Dec	− 5.3	Q3	na	na	108.1	105.7	1.41	1.47	2.65	1.83	1.35	+ 2.9
Norway	+ 34.0	Dec	+ 33.8	Nov	na	na	98.2	92.5	6.34	6.98	11.9	8.26	6.10	+ 8.2
Portugal	− 17.9	Oct	− 12.6	Nov	na	na	93.7**	93.2	0.77	0.80	1.45	–	0.74	− 2.9

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, November average. ‡OECD estimate.
**IMF, September average.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Household debt

Feb 3rd 2005
From The Economist print edition



Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Overview

Feb 3rd 2005
From The Economist print edition

In the year to December, industrial production rose by 4.5% in **South Korea** and by 3.0% in **Thailand**.

Consumer-price inflation in **India** slowed to 3.8% in the year to December from 4.2% in the year to November.

GDP growth in **the Philippines** slowed to 5.4% in the year to the fourth quarter from 6.3% in the year to the third quarter.

Peru's industrial production rose by 10.8% in the year to November.

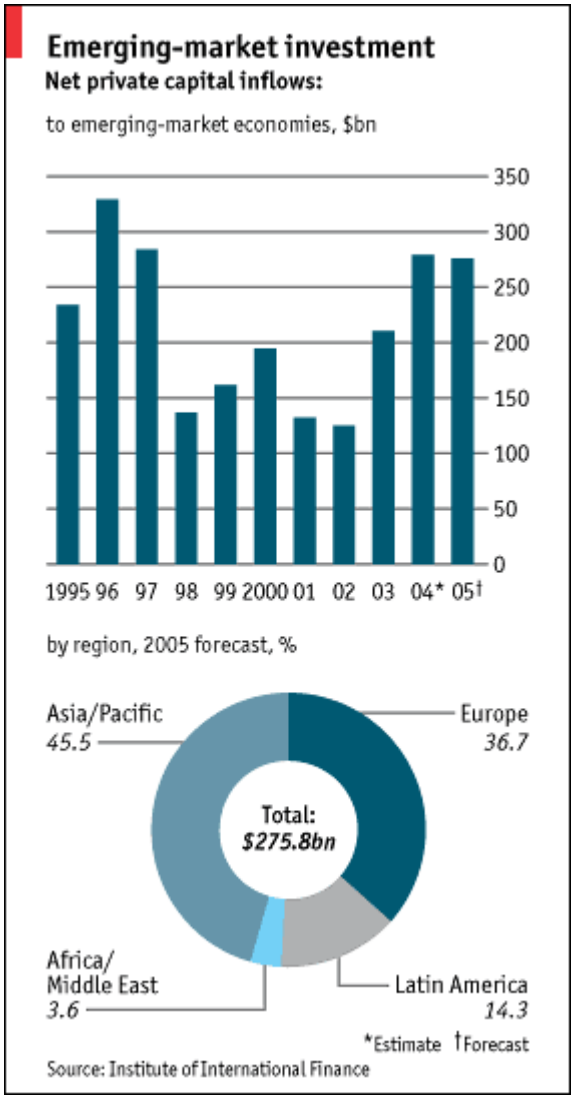
In the year to January, consumer-price inflation in **Colombia** ran at 5.4%; in **Venezuela**, by contrast, prices surged by 18.5%.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Emerging-market investment

Feb 3rd 2005
From The Economist print edition

Capital is again flowing briskly to developing countries, according to the Institute of International Finance (IIF). Emerging economies received $279 billion in private capital in 2004, a 32% increase from 2003 and the highest level since 1997. Direct investments and commercial bank loans accounted for most of the gain. The IIF reckons that Latin America will see the fastest growth in inflows this year, while flows to Asia will slow. African and Middle Eastern countries are likely to receive just 4% of the total net private capital bound for emerging economies.



Economy

Feb 3rd 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q4	+14.4	Dec	+ 2.4	Dec	+31.9	Dec	+45.9	2003	609.9	Dec
Hong Kong	+ 7.2	Q3	+ 3.4	Q3	+ 0.2	Dec	–12.1	Dec	+14.2	Q3	123.6	Dec
India	+ 6.6	Q3	+ 7.9	Nov	+ 3.8	Dec	–22.2	Dec	+ 3.5	Q3	125.2	Dec
Indonesia	+ 5.0	Q3	– 2.3	Aug	+ 7.3	Jan	+24.1	Dec	+ 4.0	Q3	35.0	Dec
Malaysia	+ 6.8	Q3	+ 9.9	Nov	+ 2.1	Dec	+21.2	Nov	+14.7	Q3	65.9	Dec
Philippines	+ 5.4	Q4	+ 8.7	Nov	+ 7.9	Dec	– 0.8	Nov	+ 4.4	Sep	12.9	Dec
Singapore	+ 5.4	Q4	+31.7	Dec	+ 1.5	Dec	+15.8	Dec	+29.0	Q3	112.8	Dec
South Korea	+ 4.6	Q3	+ 4.5	Dec	+ 3.1	Jan	+30.2	Jan	+27.6	Dec	199.0	Dec
Taiwan	+ 5.3	Q3	– 0.9	Dec	+ 1.6	Dec	+ 6.1	Dec	+24.8	Q3	241.7	Dec
Thailand	+ 6.0	Q3	+ 3.0	Dec	+ 2.7	Jan	+ 1.7	Dec	+ 7.3	Dec	47.1	Nov
Argentina	+ 8.3	Q3	+ 5.4	Nov	+ 6.1	Dec	+12.1	Dec	+ 3.6	Q3	19.6	Dec
Brazil	+ 6.1	Q3	+ 8.1	Nov	+ 7.6	Dec	+34.3	Jan	+10.7	Nov	52.9	Dec
Chile	+ 6.8	Q3	+ 9.9	Nov	+ 2.4	Dec	+ 8.9	Dec	+ 2.0	Q3	16.0	Dec
Colombia	+ 2.4	Q3	+ 1.4	Oct	+ 5.4	Jan	+ 0.9	Oct	– 1.4	Q3	12.2	Dec
Mexico	+ 4.4	Q3	+ 5.4	Nov	+ 5.2	Dec	– 8.1	Dec	– 5.5	Q3	63.7	Nov
Peru	+ 8.4	Nov	+10.8	Nov	+ 3.5	Dec	+ 2.5	Nov	– 0.3	Q3	11.5	Nov
Venezuela	+15.8	Q3	+14.7	Oct	+18.5	Jan	+21.5	Q3	+14.4	Q3	17.2	Oct
Egypt	+ 4.3	2004†	+ 3.3	2004‡	+11.7	Nov	– 8.1	Q3	+ 4.1	Q3	13.5	Sep
Israel	+ 3.4	Q3	+13.7	Nov	+ 1.2	Dec	– 6.8	Dec	+ 0.5	Q3	27.0	Dec
South Africa	+ 3.8	Q3	+ 2.3	Nov	+ 3.4	Dec	– 1.9	Dec	– 4.7	Q3	13.2	Dec
Turkey	+ 4.5	Q3	+ 9.6	Nov	+ 9.3	Dec	–34.2	Nov	–15.7	Nov	36.0	Dec
Czech Republic	+ 3.6	Q3	+10.9	Nov	+ 2.8	Dec	– 1.2	Nov	– 6.4	Q3	28.5	Dec
Hungary	+ 3.7	Q3	+ 7.9	Nov	+ 5.5	Dec	– 2.5	Q3	– 8.6	Q3	15.2	Nov
Poland	+ 4.8	Q3	+ 6.4	Dec	+ 4.4	Dec	– 6.1	Nov	– 3.0	Dec	35.3	Dec
Russia	+ 6.4	Q3	+ 4.8	Dec	+11.7	Dec	+87.0	Dec	+49.5	Q3	120.8	Dec
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 6.1	Q3	+ 4.5	Nov	+ 5.0	Dec	– 2.7	Nov	– 1.5	Q3	1.6	Nov
Latvia	+ 9.1	Q3	+ 6.0	Nov	+ 7.3	Dec	– 2.7	Nov	– 1.7	Nov	1.8	Nov
Lithuania	+ 5.8	Q3	na		+ 2.9	Dec	– 3.2	Nov	– 2.0	Q3	3.6	Nov
Slovakia	+ 5.3	Q3	+ 2.5	Nov	+ 5.9	Dec	– 1.2	Nov	– 0.9	Sep	13.4	Nov
Slovenia	+ 4.9	Q3	+ 3.8	Nov	+ 3.2	Dec	– 1.5	Nov	– 0.1	Nov	8.2	Oct
Pakistan	+ 6.4	2004†	+18.6	Jul	+ 7.4	Dec	– 5.0	Dec	+ 0.8	Q3	9.8	Dec
Saudi Arabia	+ 7.2	2003	na		+ 0.4	Oct	+59.1	2003	+28.0	2003	23.6	Nov

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡Year ending June, new series.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

Financial markets

Feb 3rd 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Feb 2nd		Dec 31st 2003	
	Feb 2nd	year ago	Feb 2nd	% a year		one week	in local currency	in $ terms
China	8.28	8.28	15.6	3.30	1,315.2	+0.9	– 16.2	– 16.2
Hong Kong	7.80	7.78	14.7	1.08	13,555.8	–0.5	+ 7.8	+ 7.3
India	43.3	45.3	81.6	5.31	6,530.1	+6.0	+ 11.8	+ 17.8
Indonesia	9,185	8,450	17,311	7.56	1,052.8	+1.5	+ 52.2	+ 39.5
Malaysia	3.80	3.80	7.16	2.82	918.5	–0.5	+ 15.7	+ 15.7
Philippines	55.0	56.1	103.6	6.19	1,989.7	+1.0	+ 37.9	+ 39.3
Singapore	1.64	1.69	3.08	1.78	2,108.7	+1.0	+ 19.5	+ 24.0
South Korea	1,028	1,168	1,937	3.58	921.4	–0.6	+ 13.7	+ 31.8
Taiwan	31.7	33.2	59.7	1.35	6,018.7	+3.1	+ 2.2	+ 9.6
Thailand	38.5	39.0	72.6	2.45	710.3	+1.1	– 8.0	– 5.3
Argentina	2.93	2.94	5.52	4.44	1,371.0	+1.2	+ 27.9	+ 28.2
Brazil	2.62	2.91	4.94	18.24	24,605.4	+0.3	+ 10.7	+ 21.7
Chile	582	590	1,096	2.76	8,845.4	+1.0	+ 20.6	+ 22.8
Colombia	2,362	2,749	4,451	7.64	4,579.5	+6.1	+ 96.2	+131.0
Mexico	11.2	11.0	21.0	9.07	13,339.4	+2.3	+ 51.7	+ 52.7
Peru	3.26	3.49	6.14	3.04	3,877.9	–1.4	+ 59.3	+ 69.3
Venezuela	2,754§	2,977§	5,190	14.74	29,711.0	+1.7	+ 33.8	+ 38.6
Egypt	5.82	6.17	10.96	9.90	32,084.5	+11.3	+175.7	+192.3
Israel	4.39	4.49	8.28	1.00	665.3	+2.0	+ 24.5	+ 24.5
South Africa	6.04	6.90	11.4	7.55	12,957.7	+2.8	+ 24.7	+ 37.9
Turkey	1.35**	1.33**	2.54	19.78	27,936.5	+3.3	+ 50.0	+ 56.8
Czech Republic	23.1	26.5	43.5	2.29	1,102.7	+0.4	+ 67.3	+ 86.3
Hungary	188	212	354	8.77	15,462.9	+1.6	+ 64.8	+ 82.1
Poland	3.09	3.83	5.82	6.60	26,231.1	+2.5	+ 26.0	+ 52.8
Russia	28.0	28.5	52.7	13.00	651.0‡	+7.5	+ 9.8	+ 14.8
EMF (MSCI)*	1.00	1.00	1.88	na	543.4	+2.0	+ 22.7	+ 22.7
EMBI+†	1.00	1.00	1.88	na	331.6	+0.3	+ 12.5	+ 12.5

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate. **New lira.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.